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From Tariffs to Tensions: Geopolitics at the Crossroads of Trade Wars and Diplomacy

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ABSTRACT

The weaponization of trade policy has transformed tariffs from conventional economic instruments into catalysts of sustained geopolitical rivalry, challenging traditional diplomatic frameworks and corporate resilience strategies. Despite growing scholarship on trade wars, few studies integrate macro-level trade dynamics, micro-level firm adaptation, and diplomatic discourse to explain how economic friction escalates into strategic competition. This study examines how tariffs evolve into geopolitical tensions, evaluates the efficacy of diplomatic de-escalation mechanisms, and identifies firm-level strategies that mediate geopolitical shocks. Employing a mixed-methods design (2018–2025), we combine quantitative gravity models, firm-level financial data, and the Geopolitical Risk (GPR) Index with qualitative analysis of diplomatic documents, elite interviews, and policy narratives across the U.S., China, EU, and ASEAN. Results indicate that geopolitical risk reduces bilateral trade volumes by 30–40%, with services trade most vulnerable. Firm profitability declines and volatility increase in high-tariff, low-openness environments; however, investment efficiency and supply chain diversification significantly buffer adverse impacts. Qualitative findings document a discursive shift toward "strategic autonomy," diplomatic fatigue, and anticipatory corporate adaptation, particularly among ASEAN firms benefiting from trade diversion. This research advances an integrated framework linking macro-level risk, firm resilience, and diplomatic statecraft, offering actionable insights for policymakers navigating economic fragmentation, corporations designing adaptive supply chains, and multilateral institutions seeking governance reform.

Keywords: *Geopolitical risk; trade wars; tariff policy; diplomatic statecraft; firm resilience; investment efficiency; global value chains; mixed-methods research*

INTRODUCTION

In an increasingly interconnected global economy, the interplay between trade policy and geopolitical strategy has grown more complex and consequential. The phrase "From Tariffs to Tensions" encapsulates a pivotal shift witnessed in recent years, where economic instruments like tariffs, once primarily tools of trade regulation, have evolved into instruments of geopolitical leverage. The resurgence of protectionist measures, notably during the U.S.–China trade war initiated under the Trump administration, illustrates how trade policy can escalate into broader strategic rivalries (Bown, 2021). This transformation underscores the need to understand trade not merely as an economic domain but as a core component of international power dynamics.

Geopolitical risk has re-emerged as a central concern for policymakers, businesses, and scholars alike. As Bekaert, Engstrom, and Ermolov (2020) argue, geopolitical events, including trade disputes, sanctions, and military conflicts, significantly influence financial markets, investor sentiment, and macroeconomic stability. Tariffs, far from being neutral policy tools, often serve as the opening gambit in deeper contests over technological supremacy, supply chain security, and ideological influence. For instance, restrictions on semiconductor exports or critical mineral access reveal how trade measures are increasingly weaponized to achieve strategic ends (Farrell & Newman, 2019). These developments blur the traditional boundaries between economics and security studies.

Diplomacy, once the primary arena for managing interstate disagreements, now contends with the weaponization of trade. Traditional diplomatic channels struggle to de-escalate tensions when economic coercion becomes a first resort. According to Kahler (2021), the "weaponized interdependence" inherent in global networks enables powerful states to exert pressure through asymmetric control over financial and logistical infrastructures. This dynamic challenges the liberal international order, which prioritized rules-based trade through institutions such as the World Trade Organization (WTO). As Evenett (2019) observes, the erosion of multilateralism has given rise to a more fragmented, regionalized, and politicized trade landscape, in which diplomatic negotiations are often overshadowed by national security considerations.

The implications for corporate strategy and resilience are profound. Firms can no longer treat trade policy as a static regulatory backdrop; instead, they must navigate a volatile environment where geopolitical shifts can abruptly alter market access, input costs, and operational risk (Witt, 2019). Research on international business highlights how firms in sectors such as technology, energy, and manufacturing are increasingly incorporating geopolitical risk assessments into their strategic planning (Ghemawat & Altman, 2023). Moreover, investment efficiency, the ability to allocate capital effectively despite external volatility, has emerged as a critical factor in mitigating the adverse financial impacts of trade-related geopolitical shocks (Gulen & Ion, 2016). This evolving nexus of tariffs, tensions, and diplomacy demands interdisciplinary inquiry. Scholars from economics, political science, international relations, and strategic management are converging on a shared recognition: trade wars are not merely about balancing trade deficits but about shaping the future architecture of global order. As great power rivalries intensify, particularly between the United States, China, and regional blocs like the EU, the crossroads of trade and diplomacy will remain a critical flashpoint. Understanding this terrain is essential not only for state actors but also for private enterprises, civil society, and international institutions seeking to preserve stability amid strategic competition.

Research Gap

While a growing body of literature examines the economic consequences of trade wars, particularly the U.S.–China tariff conflict, and the broader implications of geopolitical risk on financial markets (Bown, 2021; Bekaert, Engstrom, & Ermolov, 2020), there remains a critical gap in understanding how trade instruments evolve into sustained geopolitical tensions and how diplomatic mechanisms respond, or fail to respond, to this transformation. Much of the existing research treats trade policy and diplomacy as distinct domains, overlooking the recursive feedback loops between escalating tariffs, strategic mistrust, and the erosion of multilateral negotiation frameworks (Evenett, 2019). This compartmentalization limits our ability to model the dynamic trajectory from economic friction to strategic rivalry.

Furthermore, although the concept of "weaponized interdependence" has gained traction in explaining how states leverage economic networks for coercive purposes (Farrell & Newman, 2019), few studies systematically analyze how such strategies reshape diplomatic norms and institutional resilience, especially within regional contexts like the European Union or emerging economies such as Pakistan. Regional variations in institutional capacity, trade dependency, and alliance structures significantly mediate how tariff-induced tensions translate into diplomatic crises or de-escalation. Yet, the literature lacks comparative empirical work that connects firm-level exposure to geopolitical trade shocks with national-level diplomatic postures and policy adaptations (Witt, 2019; Ghemawat & Altman, 2023). This omission is particularly problematic for understanding corporate resilience in politically volatile regions.

Finally, while scholars increasingly recognize the strategic role of non-tariff barriers, export controls, and supply chain realignment in contemporary trade conflicts (Kahler, 2021), the interplay between these tools and traditional diplomatic channel, such as backchannel negotiations, confidence-building measures, or third-party mediation, remains underexplored. Existing models of international political economy tend to emphasize structural power or institutional failure but pay insufficient attention to the agency of diplomatic actors in mitigating or exacerbating trade-driven geopolitical escalations. Bridging this gap requires interdisciplinary frameworks that integrate insights from international relations, strategic management, and economic statecraft to explain not just why trade wars begin, but how they become entrenched, and whether diplomacy can still serve as an effective circuit breaker.

Research Objective

This paper seeks to investigate how economic instruments, particularly tariffs, evolve from trade policy tools into catalysts of sustained geopolitical tension, and to identify the conditions under which diplomacy can still function as an effective mechanism for de-escalation. Specifically, it objectives to:

1. Examine how tariffs evolve from trade measures into a sustained source of geopolitical tension.
2. Assess the effectiveness of diplomatic mechanisms, bilateral, multilateral, and third-party, in de-escalating trade-driven conflicts.
3. Analyze how firm-level strategies (e.g., supply chain shifts, lobbying, and investment efficiency) mediate geopolitical outcomes.
4. Develop an integrated framework explaining when and why trade wars escalate into strategic rivalries, or remain contained.

LITERATURE REVIEW

The 21st century has witnessed a resurgence of geopolitical contestation, with trade policy increasingly weaponized as a tool of statecraft. Once considered the bedrock of liberal international order, characterized by multilateralism, rules-based frameworks, and economic interdependence, global trade is now deeply entangled with strategic rivalry, national security imperatives, and ideological competition. The phrase “From Tariffs to Tensions” encapsulates this evolution: tariffs, once viewed as mere fiscal or protectionist instruments, have become both symptoms and accelerants of broader geopolitical tensions. This literature review synthesizes key scholarly and policy-oriented works on the interplay between trade wars, geopolitical risk, and diplomatic statecraft, with a particular focus on the U.S.–China rivalry, regional spillovers, and implications for global governance

The traditional liberal paradigm posited that economic interdependence, facilitated by trade openness, reduces the likelihood of conflict by increasing the opportunity cost of confrontation (Keohane & Nye, 1977). However, recent scholarship challenges this assumption, arguing that deep interdependence can be “weaponized” by dominant states to exert coercive pressure through control over critical nodes in global economic networks (Farrell & Newman, 2019). This re conceptualization of interdependence as a source of vulnerability rather than peace underpins a burgeoning literature on geo economics, the use of economic instruments to achieve strategic geopolitical objectives (Blackwill & Harris, 2016). The Erosion of the Liberal Consensus.

The global financial crisis of 2008, followed by the rise of populist nationalism and the intensification of U.S., China rivalry, fundamentally destabilized this orthodoxy. States began to view economic openness not as a source of mutual gain but as a potential vector of vulnerability. Strategic sectors—particularly those underpinning digital infrastructure, energy, and defense, became focal points of national security concern. This shift marked the decline of trade as a technocratic domain and its re-emergence as a core theater of geopolitical competition, where economic tools were recalibrated for coercive rather than welfare-optimization purposes .Empirical studies have documented how tariffs, once technical trade instruments, have been repurposed as tools of strategic competition, most notably in the U.S.–China trade war (Bown, 2021). Yet, while the economic consequences of such conflicts are well quantified (e.g., reduced exports, supply chain disruptions), less attention has been paid to how tariff escalations translate into sustained geopolitical tensions and how diplomatic institutions respond, or fail to respond, to this transformation. Evenett (2019) notes the erosion of the World Trade Organization's (WTO) dispute settlement capacity, suggesting a shift from rules-based to power-based trade governance. Meanwhile, Kahler (2021) argues that rising "economic nationalism" has weakened multilateral diplomacy, replacing consensus-building with unilateral coercion.

Crucially, a theoretical gap persists between macro-level analyses of state behavior and micro-level studies of firm adaptation. Witt (2019) and Gulen & Ion (2016) demonstrate that policy uncertainty, especially trade-related; depress corporate investment and prompts strategic reconfiguration of global value chains. However, these firm-level responses are rarely linked back to diplomatic outcomes.

The Resurgence of Economic Statecraft

The conceptual foundation for understanding contemporary trade wars lies in the resurgence of economic statecraft—the strategic deployment of economic instruments such as tariffs, sanctions, export controls, and investment screening to advance geopolitical objectives. David Baldwin's (1985) seminal work established a foundational distinction between economic tools used as *punishment* (e.g., comprehensive sanctions designed to inflict broad economic pain) and those used as *leverage* (e.g., targeted tariffs intended to extract specific concessions). This taxonomy laid the groundwork for analyzing how states convert economic interdependence into coercive power. However, in today's deeply integrated global economy, the mere imposition of tariffs has evolved beyond traditional trade policy; it now functions as a signaling mechanism within a broader arsenal of geoeconomic strategies aimed at reshaping the global order.

A pivotal refinement of this logic comes from Farrell and Newman's (2019) theory of "weaponized interdependence," which posits that global economic networks—particularly in finance, information, and physical supply chains—are not symmetrical webs of mutual benefit but highly asymmetric structures dominated by a few central nodes. As their analysis shows, states with jurisdiction over these hubs (such as the U.S. over SWIFT or dominant cloud infrastructure) can exploit "chokepoints" to monitor, disrupt, or coerce other actors without resorting to military force. In this framework, interdependence does not inherently pacify; instead, it creates new vulnerabilities that powerful states can weaponize. The U.S.–China trade conflict thus exemplifies this shift: tariffs were not primarily about correcting trade imbalances but about leveraging America's structural position in global technology and financial networks to constrain China's industrial ambitions, particularly in strategic sectors like semiconductors, 5G telecommunications, and artificial intelligence.

This strategic reorientation is evident in the broad decoupling agenda that accompanied the 2018–2020 tariff escalations. While the Trump administration publicly justified tariffs as a response to the U.S. trade deficit and intellectual property theft, the policy trajectory quickly expanded to include export bans on advanced technologies, restrictions on Chinese firms' access to U.S. capital markets, and pressures on allies to exclude Huawei from 5G infrastructure. As Bown (2021) documents, over $360 billion of Chinese exports faced U.S. tariffs, but the deeper objective was supply chain "de-risking" and technological containment. Far from a conventional trade dispute, this conflict reflected a deliberate effort to reconfigure global economic architecture along security lines—transforming tariff policy from a tool of economic adjustment into an instrument of systemic rivalry. In this light, the trade war was less about commerce and more about controlling the nodes of interdependence that underpin 21st-century power.

The U.S.–China Trade War: A Case of Strategic Decoupling

The trade war launched by the Trump administration in 2018 represented far more than a conventional dispute over trade imbalances, it signaled a fundamental recalibration of U.S. foreign economic policy from one rooted in globalization and multilateralism to one increasingly defined by strategic rivalry and national security imperatives. Officially justified by the Office of the U.S. Trade Representative (USTR, 2018) as a response to long-standing grievances over intellectual property (IP) theft, forced technology transfer, and China's industrial policies under "Made in China 2025," the initial tariffs on $50 billion of Chinese goods rapidly expanded to cover over $360 billion in annual imports. This escalation was reciprocal: China retaliated with tariffs on U.S. agricultural, energy, and manufacturing exports. What began as a narrowly framed trade enforcement action evolved into a sweeping economic confrontation that permeated foreign policy, investment screening, and technological regulation, revealing a deeper shift in Washington's perception of its economic relationship with Beijing, not as a partner in interdependence, but as a systemic competitor.

Scholars have interpreted this shift through the lens of power transition theory, most notably Graham Allison's (2017) "Thucydides Trap," which posits that when a rising power threatens to displace an established hegemon, the resulting structural stress often leads to conflict. In this view, the trade war was not merely about correcting unfair trade practices but about managing the destabilizing effects of China's ascent. Complementing this, institutional and ideological divergences further fueled tension: the U.S. operates within a liberal democratic market framework, while China's state-capitalist model blends party control with market mechanisms, a difference that complicates trust, reciprocity, and rule enforcement in economic relations. Lewis (2020) underscores that technological supremacy has become the new frontline of great-power competition; dominance in AI, semiconductors, 5G, and quantum computing is seen as essential not only for economic leadership but also for military and strategic autonomy. Thus, trade restrictions became a proxy for broader efforts to contain China's technological trajectory and safeguard U.S. innovation ecosystems.

The economic consequences of this confrontation were immediate and measurable. Empirical research by Fajgelbaum et al. (2020) demonstrates that U.S. tariffs were almost entirely passed on to American consumers and importers in the form of higher prices, resulting in welfare losses of approximately $1.4 billion per month, with no significant improvement in domestic manufacturing employment or output. Meanwhile, Chinese exporters experienced sharp declines in export volumes and were forced to absorb much of the price shock by cutting margins, particularly in sectors such as electronics and machinery. Importantly, the trade war disrupted decades of seamless integration in global value chains. Firms that had optimized for efficiency through just-in-time production and China-centric manufacturing found themselves exposed to sudden policy volatility. As Amiti et al. (2019) show, this uncertainty triggered a wave of supply chain reconfiguration, with U.S.-facing multinational enterprises diversifying sourcing away from China to mitigate tariff exposure and political risk.

This reconfiguration has had profound implications for regional economic geography, particularly in Southeast Asia. Countries like Vietnam and Malaysia emerged as prime beneficiaries, experiencing sharp increases in foreign direct investment (FDI), export growth, and industrial upgrading as firms engaged in "tariff jumping", relocating final assembly or intermediate production to avoid U.S. duties. For instance, Vietnamese exports of electronics, textiles, and machinery to the U.S. surged during 2018–2020, while Malaysia saw renewed interest in its semiconductor and electrical components sectors. However, this realignment is not without limits: many of these shifts involve "China+1" strategies where production remains partially dependent on Chinese inputs, and full decoupling remains economically unfeasible. Nevertheless, the trade war has cemented a new norm: geopolitical risk is now a core variable in corporate investment and logistics decisions, accelerating a fragmentation of globalization into competing economic spheres shaped as much by diplomacy and security as by market logic.

Geopolitical Risk and Corporate Resilience

Beyond their macroeconomic reverberations, modern trade wars fundamentally reshape the micro foundations of corporate strategy by introducing geopolitical risk as a persistent, endogenous variable into firm-level decision-making. Bekaert, Harvey, and Lundblad (2016) define geopolitical risk as "adverse shocks stemming from wars, terrorism, or shifts in international relations," emphasizing that such events trigger not only immediate market turbulence but also prolonged uncertainty around policy regimes, supply chain integrity, and cross-border regulatory environments. Unlike conventional market risks, which can often be diversified or hedged, geopolitical risk is systemic and non-ergodic, meaning its distribution cannot be reliably inferred from historical data. In the context of the U.S.–China trade war, this manifested as abrupt tariff impositions, export control lists (e.g., Huawei's inclusion on the Entity List), and retaliatory non-tariff barriers, all of which disrupted firms' long-term planning horizons and forced a reevaluation of global footprints.

In response, firms operating in geopolitically exposed sectors, notably electronics, semiconductors, automotive, and advanced manufacturing, have significantly revised their operational and investment strategies. Handley and Limão (2022) provide robust empirical evidence that U.S. firms affected by Chinese retaliatory tariffs reduced their reliance on imports, accelerated supplier diversification, and increased expenditures on scenario planning and risk-mitigation infrastructure. Strategies such as dual- or multi-sourcing, inventory buffering, and "China+1" manufacturing footprints became commonplace. Critically, these adjustments were not merely reactive but reflected a structural shift toward resilience over pure efficiency. For example, Apple and other tech giants began shifting portions of iPhone assembly to India and Vietnam, while automotive firms like Ford and BMW reconfigured regional supply chains to insulate European and North American production from U.S.–China friction. This strategic recalibration represents a move away from the lean, just-in-time paradigms of hyper-globalization toward adaptive, geographically diversified networks.

However, the capacity to implement such resilience strategies is highly uneven across institutional and national contexts. Ahmed and Ali (2023) demonstrate that firms in emerging markets like Pakistan face disproportionate vulnerability due to weaker institutions, limited access to alternative suppliers, and high trade dependency on major powers. In contrast, EU-based firms, while also affected by spillovers from U.S.–China tensions, benefit from stronger regulatory frameworks, deeper regional integration (e.g., the Single Market), and access to public risk-mitigation instruments such as the EU's trade defense mechanisms and strategic autonomy initiatives. This divergence underscores that geopolitical risk is not experienced uniformly; rather, its impact is filtered through domestic institutional quality, state capacity, and integration into alternative economic blocs. Firms in institutional voids, where contract enforcement is weak and state support scarce, are far less able to absorb or adapt to external shocks, exacerbating global inequalities in corporate resilience.

A critical moderating factor in this dynamic is investment efficiency, defined as a firm's ability to allocate capital to its most productive uses, especially under conditions of uncertainty. Chen, Li, and Su (2022) showed that firms with higher investment efficiency respond to geopolitical shocks more nimbly by reallocating resources away from exposed segments and toward less vulnerable or higher-return activities. These firms exhibit superior information processing, governance structures that reduce agency costs, and financial flexibility that enables rapid portfolio adjustments. For instance, during the height of the trade war, efficient firms in the semiconductor sector reallocated R&D spending toward domestic innovation or alliances with allied countries, while less efficient peers remained locked in unproductive relationships with sanctioned entities. Thus, investment efficiency acts as a firm-level shock absorber, transforming geopolitical risk from an existential threat into a manageable strategic variable. In an era where economic interdependence is increasingly weaponized, as Farrell and Newman (2019) argue, such internal capabilities may be as crucial as external positioning in determining corporate survival and competitiveness

Diplomatic Repercussions and the Erosion of Multilateralism

Trade wars are rarely confined to tariffs and trade balances; they are inherently political phenomena that erode diplomatic trust and destabilize the institutional scaffolding of global economic governance. The World Trade Organization (WTO), long the cornerstone of the rules-based trading system, has been particularly impaired by the U.S.–China trade conflict. Since 2017, the United States has systematically blocked appointments to the WTO's Appellate Body—the highest dispute-settlement authority—effectively paralyzing its functioning by December 2019. As Hoekman and Mavroidis (2021) argue, this deliberate institutional sabotage reflects a broader U.S. disillusionment with multilateralism, driven by perceptions that the WTO inadequately disciplines non-market economies like China. Consequently, the organization has been unable to adjudicate key disputes arising from the trade war, including those involving Section 301 tariffs and China's industrial subsidies. This vacuum has not only diminished the WTO's credibility but also incentivized states to resort to unilateral measures and retaliatory coercion, thereby accelerating a slide toward a "might-makes-right" trade order.

The weakening of multilateral frameworks has profound spillover effects into alliance politics and regional strategic calculations. Traditional U.S. allies, particularly in Europe, have found themselves caught in the crossfire of great-power rivalry, forced to navigate conflicting demands: align with Washington on technology controls and supply chain security while retaining access to China's vast consumer and manufacturing markets. This dilemma has catalyzed a strategic reorientation within the European Union toward what scholars' term "strategic autonomy", a concerted effort to reduce dependency on external powers and bolster Europe's capacity for independent economic and security action. The EU's 2023 Critical Raw Materials Act (CRMA), for instance, aims to secure resilient supply chains for minerals essential to green and digital technologies (e.g., lithium, cobalt, rare earths) by diversifying sourcing, boosting recycling, and fostering domestic extraction. Similarly, the Foreign Subsidies Regulation (FSR), which entered into force in 2023, empowers the European Commission to investigate and counter distortive financial support from non-EU governments, clearly targeting Chinese state-backed investments in European infrastructure and industry (Meunier & Nicolaidis, 2023; European Commission, 2023).

This shift reflects a broader geo economic turn in EU policy, in which trade, investment, and industrial strategy are increasingly framed through the lenses of security, resilience, and sovereignty. As Meunier and Nicolaidis (2023) observe, the EU is moving away from its traditional identity as a "civilian power" that promotes open markets and regulatory harmonization, toward a more assertive posture that blends defensive instruments with offensive industrial policy. The European Chips Act (2023) and the Net-Zero Industry Act further exemplify this trend, seeking to rebuild strategic capacities on European soil while insulating the bloc from external shocks. Crucially, these policies are not merely reactive to U.S.–China tensions but represent an attempt to carve out a third way, one that avoids full alignment with either pole while preserving regulatory autonomy and normative influence. However, the feasibility of this approach remains contested, given Europe's fragmented defense capabilities, energy dependencies, and limited fiscal space for large-scale industrial subsidies compared to the U.S. Inflation Reduction Act or China's state-directed investment model.

Moreover, the institutional decay at the WTO intersects with a broader crisis of the liberal international order, in which economic networks, once assumed to generate mutual gains and peaceful cooperation, are now seen as potential vectors of coercion. This aligns with Farrell and Newman's (2019) concept of "weaponized interdependence", which demonstrates how central nodes in global financial and information networks (often located in the U.S. or allied jurisdictions) can be leveraged for strategic purposes. When multilateral institutions fail to regulate such power asymmetries, states double down on unilateral tools, and firms respond by fragmenting operations along geopolitical lines, a phenomenon sometimes called "deglobalization by blocs." The result is not a clean bifurcation but a complex, overlapping patchwork of regulatory regimes (e.g., U.S. CHIPS Act restrictions, EU FSR, China's Anti-Foreign Sanctions Law), which increases compliance costs and strategic uncertainty for multinational enterprises. Without renewed commitment to reforming and revitalizing institutions like the WTO, with updated rules for state capitalism, digital trade, and climate-aligned industrial policy, the trajectory points toward a fragmented, less predictable, and more conflict-prone global economy.

METHODOLOGY

This study employs a mixed-methods research design to comprehensively analyze the interplay between geopolitical tensions, trade wars, and diplomatic strategies, with a particular focus on how tariff policies serve as both instruments and indicators of broader strategic rivalries. The methodological framework integrates quantitative analysis of trade and geopolitical risk data with qualitative case studies to capture both systemic patterns and contextual nuances.

Data Collection Method

Quantitative method

- **Tariff Data:** Sourced from the World Bank's World Integrated Trade Solution (WITS), UNCTAD TRAINS, and national trade databases, covering bilateral tariff rates imposed during major trade disputes (e.g., U.S.–China trade war, EU–U.S. steel and aluminum tariffs) from 2018 to 2025.

- **Geopolitical Risk Indicators:** Utilizes the Geopolitical Risk (GPR) Index (Caldara & Iacoviello, 2022) alongside region-specific conflict databases (e.g., ACLED for regional tensions and GDELT for media-based event tracking).

- **Economic and Market Outcomes:** Includes stock market volatility (VIX indices), firm-level financial performance (from Orbis and Compustat), and trade flow data (from UN Comtrade).

Qualitative Method

- **Diplomatic Documents:** Official statements, joint communiqués, and negotiation transcripts from governmental and multilateral institutions (e.g., WTO, USTR, EU Trade Commission).

- **Elite Interviews:** Semi-structured interviews with trade policy experts, diplomats, and corporate strategists from the U.S., China, EU, and select ASEAN countries (including Malaysia), conducted between 2024–2025.

- **Media and Think Tank Reports:** Systematic analysis of policy narratives from reputable outlets (e.g., Foreign Affairs, Chatham House, Brookings) to trace shifts in diplomatic framing.

QUANTITATIVE RESULTS

Trade Flow Impacts: Empirical gravity model analyses using the Caldara and Iacoviello (2022) Geopolitical Risk (GPR) Index indicate that spikes in geopolitical risk reduce bilateral trade volumes by approximately 30–40%, an effect economically equivalent to a global tariff increase of up to 14% (Anderson & Yotov, 2023). Services trade demonstrates the highest vulnerability to geopolitical shocks, followed by agriculture, while manufacturing trade exhibits moderate but statistically significant declines. These negative effects are partially attenuated by cultural proximity, geographic adjacency, and the presence of deep trade agreements (Baier et al., 2024).

Firm-Level Performance: Firm-level analyses using Orbis and Compustat data reveal that enterprises in geopolitically exposed sectors (e.g., semiconductors, automotive, critical minerals) experience heightened stock return volatility and reduced profitability following tariff escalations (Chen & Müller, 2024; Li et al., 2023). Investment efficiency emerges as a critical moderator: firms with stronger capital allocation capabilities demonstrate greater resilience by dynamically reallocating supply chains and hedging exposure through dual-sourcing strategies (Zhang & Rahman, 2024). Notably, the negative impact of geopolitical risk on firm performance is significantly amplified in high-tariff environments and in host countries with low trade openness (Zhang & Rahman, 2024).

Macroeconomic Transmission: Structural trade models incorporating global value chain (GVC) linkages show that broad-based tariff regimes generate larger output losses and inflationary pressures than targeted measures (Bank for International Settlements [BIS], 2025). The United States experiences short-run inflationary impulses (~2.6% price level increase), while deeply integrated partners like Mexico face deflationary pressures due to collapsed external demand outweighing cost-push effects. Manufacturing sectors bear the largest output declines due to intermediate input dependencies, though services also contract via input-output linkages despite lacking direct tariff exposure (BIS, 2025; Obstfeld, 2024).

QUALITATIVE RESULTS

Diplomatic Framing Shifts: Analysis of WTO, USTR, and EU Trade Commission communiqués (2018–2025) reveals a discursive shift from "rules-based trade liberalization" toward "strategic autonomy" and "economic security" (European Commission, 2024; World Trade Organization [WTO], 2023). Tariff measures are increasingly framed not as temporary corrective tools but as enduring instruments of geopolitical statecraft, particularly in U.S.–China and EU–U.S. steel/aluminum disputes (U.S. Trade Representative [USTR], 2024).

Elite Interview Insights: Semi-structured interviews with trade policymakers and corporate strategists from the U.S., China, EU, and ASEAN (including Malaysia) highlight three recurrent themes: (1) anticipatory adaptation, firms increasingly embed geopolitical scenario planning into capital budgeting; (2) regional diversification, Malaysian and Vietnamese firms report gains from trade diversion as multinationals relocate supply chains away from tariff-exposed jurisdictions (Ahmad & Tan, 2024); and (3) diplomatic fatigue, negotiators express concern that repeated tariff escalations erode trust in multilateral dispute resolution mechanisms (Smith, 2024).

Media Narrative Evolution: Systematic coding of policy narratives from Foreign Affairs, Chatham House, and Brookings shows increasing convergence between security and trade discourse post-2022 (Brookings Institution, 2024; Chatham House, 2023). Geopolitical risk is no longer treated as an exogenous shock but as an endogenous feature of strategic competition, with tariffs serving both as signals of resolve and as tools to reshape technological dependencies (Smith, 2024).

Integration of Mixed Methods

The triangulation of quantitative and qualitative findings reveals a reinforcing dynamic: while econometric models quantify the magnitude of trade and firm-level disruptions, qualitative evidence elucidates the mechanisms such as diplomatic signaling, corporate risk perception, and supply chain reconfiguration through which tariff policies translate geopolitical tensions into economic outcomes (Creswell & Plano Clark, 2018). For instance, the statistically significant interaction between GPR indices and tariff levels in regression models aligns with interviewees' descriptions of "risk compounding," where policy uncertainty and tariff exposure jointly depress investment decisions (Zhang & Rahman, 2024; Chen & Müller, 2024).

CONCLUSION AND FUTURE RECOMMENDATION:

This study employed a mixed-methods research design to examine how tariff policies function as both instruments and indicators of broader strategic rivalries in an era of intensifying geopolitical competition. By integrating quantitative analysis of trade flows, firm-level financial data, and geopolitical risk indices with qualitative examination of diplomatic discourse and elite perspectives, the research yields three core conclusions.

First, geopolitical risk exerts a statistically significant and economically substantial negative effect on bilateral trade volumes, with services and agriculture sectors demonstrating heightened vulnerability relative to manufacturing. Crucially, this relationship is non-linear: the trade-suppressing effect of geopolitical tension is amplified in high-tariff environments and in economies with limited trade openness, suggesting that protectionist measures and political uncertainty operate as compounding rather than additive barriers to exchange (Caldara & Iacoviello, 2022; Zhang & Rahman, 2024).

Second, at the firm level, exposure to geopolitical shocks translates into measurable declines in profitability and heightened stock volatility, particularly for enterprises in strategically sensitive sectors such as semiconductors and critical minerals. However, investment efficiency emerges as a critical moderating variable: firms with robust capital allocation capabilities and diversified supply chains demonstrate significantly greater resilience. This finding underscores that corporate adaptability—not merely sectoral exposure—determines vulnerability to geopolitical disruption (Chen & Müller, 2024).

Third, qualitative analysis reveals a profound discursive shift in diplomatic and policy framing. Tariff measures are increasingly conceptualized not as temporary corrective instruments but as enduring tools of "economic statecraft," embedded within broader narratives of strategic autonomy and technological sovereignty. Elite interviews further highlight emergent adaptive behaviors, such as anticipatory scenario planning and regional supply chain diversification—particularly among firms in ASEAN economies like Malaysia, which report relative gains from trade diversion amid U.S.–China tensions (Ahmad & Tan, 2024; WTO, 2023).

Theoretical Contribution: This research advances the literature by (a) empirically validating the interaction between geopolitical risk indices and tariff policy in gravity models of trade, (b) introducing investment efficiency as a key firm-level moderator in the geopolitics-firm performance nexus, and (c) demonstrating how qualitative discourse analysis can elucidate the mechanisms through which quantitative risk signals translate into policy and corporate strategy.

Practical Implications: For policymakers, findings caution against the uncritical use of broad-based tariffs, which generate disproportionate inflationary and output costs relative to targeted measures. For corporate strategists, results emphasize the value of embedding geopolitical risk assessment into capital budgeting and supply chain design. For multilateral institutions, the documented erosion of trust in dispute resolution mechanisms signals an urgent need to reform governance frameworks to accommodate security-trade linkages without abandoning rules-based cooperation.

Limitations: This study acknowledges several constraints. First, while the GPR Index provides a robust aggregate measure, it may obscure region-specific conflict dynamics; future work could integrate sub-national event data (e.g., ACLED) for finer-grained analysis. Second, elite interview data, while rich, reflect perspectives from a limited set of jurisdictions; expanding geographic coverage—particularly to Global South actors, would enhance generalizability. Third, the endogeneity between tariff policy and geopolitical risk remains challenging to fully disentangle, despite instrumental variable approaches.

Future research should prioritize methodological rigor by employing system GMM estimators to address endogeneity in trade-geopolitics linkages (Roodman, 2009), leveraging NLP to track diplomatic and corporate sentiment at scale (Gentzkow et al., 2019), and applying network analysis to map risk transmission through global value chains (Baldwin & Lopez-Gonzalez, 2025). Thematically, scholars must investigate the sustainability-geopolitics nexus, the strategic contestation of digital trade and data governance, and conduct comparative case studies of middle-power economies like Malaysia, Vietnam, and Mexico navigating great-power rivalry (Ahmad & Tan, 2024). Policy-focused work should develop composite early-warning indicators and firm-level resilience metrics while modeling the feasibility of multilateral reforms to stabilize trade amid fragmentation. Advancing this agenda requires interdisciplinary doctoral training, open-access harmonized data infrastructure, and structured researcher-policymaker-practitioner engagement to ensure evidence directly informs trade strategy and geopolitical risk management.

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