World Economy Brief

March 12, 2026 | Vol. 16 No. 07 | ISSN 2233-9140

The Structural Transformation of U.S. Foreign Economic Policy and Its Economic Effects

Gusang KANG Research Fellow, North America and Europe Team, Center for East Asian and Advanced Economy Studies (gskang@kiep.go.kr)

I. Introduction

Over the past decade, U.S. foreign economic policy has undergone a structural transformation that extends beyond partisan political cycles. What initially appeared to be a temporary shift toward protectionism under the first Trump administration has consolidated into a broader orientation centered on economic security, strategic competition with China, and domestic industrial revitalization. The renegotiation of the existing trade agreements, withdrawal from multilateral frameworks, and imposition of Section 232 and Section 301 tariffs marked a clear departure from the liberal trade order that had characterized U.S. policy for decades. Rather than reversing this trajectory, the Biden administration utilized core tariff measures and expanded industrial policy through the CHIPS and Science Act and the Inflation Reduction Act, reinforcing a production-centered strategy aimed at reshaping global supply chains.

At the core of this transformation lies a reconfiguration of incentives governing global capital allocation and trade patterns. The Tax Cuts and Jobs Act (TCJA) fundamentally restructured the U.S. international tax regime through provisions such as GILTI, FDII, and BEAT while lowering the statutory corporate tax rate, thereby altering firms' location and investment decisions. At the same time, Section 301 tariffs sought to change relative prices in global value chains, reduce U.S. dependence on China, and induce supply chain realignment. Together, these measures illustrate how U.S. foreign economic policy increasingly integrates trade, tax, and industrial instruments

into a coherent framework of economic statecraft.

Against this backdrop, this report empirically evaluates the economic effects of these policy instruments. It examines how the TCJA affected U.S. outward and inward foreign direct investment and how Section 301 tariffs influenced trade flows at the product level, particularly with respect to trade diversion involving Korea. By employing panel regression and event-study methodologies, the study aims to identify causal impacts and dynamic adjustment patterns. The findings provide evidence that recent U.S. foreign economic policy has produced measurable structural effects on global investment and trade flows, offering important implications for Korea's strategic economic positioning.

II. Economic Impacts of U.S. Foreign Economic Policy

1. TCJA and Foreign Direct Investment

The Tax Cuts and Jobs Act (TCJA) reduced the statutory corporate tax rate and introduced structural changes to the U.S. international tax system through provisions such as GILTI, FDII, and BEAT. These reforms were intended to discourage profit shifting, incentivize domestic production, and reshape multinational investment incentives. The key empirical objective of this section is to identify whether the reform generated a differential change in U.S. foreign direct investment relative to comparable economies and to examine the dynamic adjustment pattern before and after implementation.

To capture these dynamic effects, the analysis employs an event-study framework within a bilateral panel setting. This approach allows the estimation of year-by-year deviations in U.S. FDI relative to a pre-reform benchmark while controlling for time-invariant bilateral characteristics and global shocks. The specification is given by:

$$\ln(FDI_{i,j,t}) = \alpha_0 + \sum_{d \neq -1} \beta_d \mathbf{1}(t - T_{TCJA} = d) + \alpha_1 \ln GDP_{i,t}$$

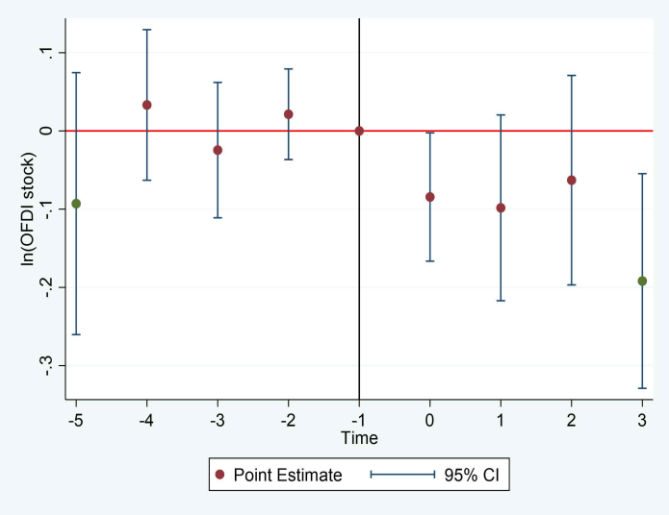
$$+ \alpha_2 \ln GDP_{j,t} + \alpha_3 \ln Dist_{i,j} + \alpha_4 CITRDiff_{i,j,t} + \gamma_{i,j} + \delta_t + \varepsilon_{i,j,t}$$

where $FDI_{i,j,t}$ denotes bilateral FDI stock between country i and j at time t, and the indicator $\mathbf{1}(t - T_{TCJA} = d)$ captures each lead and lag relative to the year prior to the reform. Country-pair fixed effects $\gamma_{i,j}$ control for persistent bilateral factors, while year fixed effects δ_t absorb common macroeconomic shocks. The exclusion of $d = -1$ provides the pre-reform reference period.

The event-study results indicate that U.S. outward FDI declined significantly relative to peer economies following the TCJA, with negative coefficients emerging immediately after implementation and persisting over subsequent years. The absence of statistically significant pre-trends supports the identification assumption. In contrast, inward FDI exhibits a

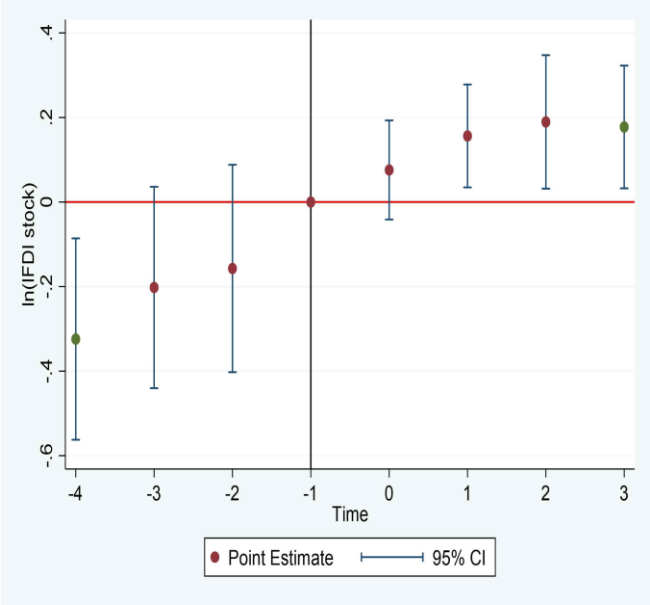
delayed but positive and statistically significant response after the reform, suggesting an improvement in the relative attractiveness of the United States as an investment destination. Overall, the dynamic estimates point to a reorientation of global investment flows toward the United States.

Figure 1. TCJA Impacts on U.S. Outward FDI



Source: Author's estimation

Figure 2. TCJA Impacts on U.S. Inward FDI



Source: Author's estimation

2. Section 301 Tariffs and Trade Diversion Effects

The second empirical analysis evaluates the impact of Section 301 tariffs imposed on Chinese imports and examines whether these measures generated trade diversion toward Korea. The objective is to estimate the elasticity of U.S. imports with respect to tariff changes at the HS product level and to identify heterogeneity across products.

Using product-level panel data, the following specification is estimated:

$$\ln IMP_{c,i,t} = \alpha + \beta_p^{CHN}\left(CHN\_TARIFF_{i,t} \times 1(c = CHN)\right) + \beta_p^{KOR}\left(CHN\_TARIFF_{i,t} \times 1(c = KOR)\right) + \delta_{c,i} + \tau_{y(t)} + \varepsilon_{c,i,t}$$

where $IMP_{c,i,t}$ denotes U.S. imports from country c in product i at time t, and $CHN\_TARIFF_{i,t}$ represents the tariff rate imposed by the United States on Chinese imports of product i. The interaction terms allow the estimation of differential tariff effects on Chinese and Korean exports to the U.S. market. The coefficient β_p^{CHN} captures the elasticity of Chinese exports with respect to tariff increases, while β_p^{KOR} measures the corresponding response of Korean exports. Country-product fixed effects $\delta_{c,i}$ control for time-invariant exporter-product characteristics, and year fixed effects $\tau_{y(t)}$ absorb common macroeconomic shocks and aggregate demand fluctuations. Standard errors are clustered at the panel level to account for serial correlation.

The estimation results indicate a statistically significant trade diversion effect. An increase in U.S. tariffs on Chinese goods reduces Chinese exports to the United States while increasing Korean exports (Table 1). However, product-level heterogeneity is substantial (Table 2). In several intermediate goods sectors, including automobile parts and industrial machinery, both Chinese and Korean exports decline simultaneously, suggesting complementary supply chain linkages rather than pure substitution effects. These findings underscore that tariff-induced adjustments operate not only through relative price effects but also through global value chain interdependencies.

Table 1. Effects of U.S. Tariff Increases on China

Category	β_p^{CHN}	β_p^{KOR}
Estimated Coefficient	-1.081	1.602
Standard Error	0.503	0.535
p-value	0.032	0.003
Observations (N)	2,059,560	
Number of Panels	19,083	

Source: Author's estimation

Table 2. Products for Which Both Chinese and Korean Exports to the U.S. Declined

HS4 Code	Product Description	Change in U.S. Imports (2016–2024, USD bn) – China	Change in U.S. Imports (2016–2024, USD bn) – Korea	Estimated Import Change Relative to 2016 – China	Estimated Import Change Relative to 2016 – Korea	Effective Tariff on China (2024, %)
8708	Motor Vehicle Parts	2.9	18.6	-92.9	-35.6	0.3
9401	Seats	-28.4	1.1	-66.3	-2.2	0.2
8479	Other Industrial Machinery	4.9	18.1	-18.7	-2.2	0.2
8421	Centrifuges, Filters, Purifiers	4.6	4.8	-13.0	-2.0	0.2
8415	Air Conditioning Machines	5.4	0.8	-19.1	-1.9	0.1
9405	Lamps and Lighting Fittings	-34.0	-0.3	-147.1	-1.6	0.3
4016	Other Vulcanized Rubber Products	0.2	-0.2	-3.6	-1.0	0.2
8428	Lifts, Elevators, Conveyors, etc.	3.1	9.6	-5.1	-0.9	0.2
7106	Silver	-0.5	2.6	-3.5	-0.9	0.2
3402	Organic Surface-Active Agents	0.3	0.4	-2.6	-0.9	0.3
5703	Carpets and Other Textile Floor Coverings	-1.2	0.3	-7.7	-0.8	0.3

Source: Author's calculation

III. Policy Implications

The structural consolidation of U.S. economic nationalism implies that Korea must prepare for a prolonged period of policy uncertainty and strategic recalibration in bilateral economic relations. The persistence of tariff measures and the integration of trade, tax, investment, and industrial policy tools suggest that U.S. foreign economic policy has entered a structural phase rather than a temporary cyclical shift.

In the trade domain, Korea should strengthen coordination with economies that share an interest in preserving a rules-based multilateral system. Enhanced cooperation with the European Union and Japan would help mitigate risks associated with unilateral trade measures and improve collective bargaining capacity. Efforts to restore the WTO dispute settlement mechanism and reinforce international trade norms should accompany such coordination.

In the investment domain, the observed reorientation of global FDI toward the United States underscores the importance of establishing a systematic monitoring framework capable of tracking changes in U.S. tax, subsidy, and regulatory policies at both the industry and firm levels. Policy finance institutions should expand their role in providing information, risk mitigation tools, and targeted financial support for Korean firms investing in strategic sectors in the United States.

More broadly, Korea should pursue institutionalized economic security cooperation with the United States. Strengthening supply chain early warning systems, deepening joint industrial policy initiatives in strategic sectors, and establishing comprehensive economic security dialogue mechanisms would enhance predictability and resilience. Embedding bilateral cooperation within formal legislative and institutional frameworks would provide a more stable foundation for long-term economic partnership.

In sum, U.S. foreign economic policy has entered a phase of structural transformation characterized by the integration of tariffs, tax reform, investment regulation, and industrial subsidies. For Korea, the policy challenge lies not merely in responding to individual measures but in designing a coherent strategic framework that anticipates the durability of this shift and aligns national industrial and trade policies accordingly.KIEP