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Trump's Greenland tariffs:

A step too far?

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President Trump's Greenland-linked tariffs could risk a rapid escalation into a global trade conflict, and financial markets will be a key signal of whether the confrontation fizzles quickly or spirals into a destabilising economic shock.

Key takeaways

- By tying tariffs to the Greenland dispute, the US may have transformed a diplomatic disagreement into a material economic threat, raising the risk that a targeted measure could quickly broaden into a systemic shock.
- If the EU retaliates, the conflict could shift from a contained US-Europe tariff dispute to a broad, global trade war – creating a large stagflationary shock that we think could hit growth and inflation simultaneously and shift the policy calculus for central banks.
- Market sentiment will be pivotal: if investors expect Europe to capitulate, economic damage may be limited in our view – whereas a negative market reaction could rapidly raise the cost of escalation for Washington and empower voices in Congress or the courts seeking to rein in the administration.

What has happened?

On Saturday 17 January, US President Trump announced a 10 percentage point tariff increase, effective 1 February, on imports from eight European countries – Germany, the UK, France, the Netherlands, Sweden, Denmark, Finland and Norway – seen as opposing his plans to acquire Greenland.

This move would raise the tariff rate to 20% for the UK and 25% for the others. Mr Trump added that if the US failed to acquire Greenland by June, the tariffs would rise by a further 15 percentage points.

At the time of writing, several practical issues remain unclear:

- **Targeting EU member states?** – Imposing tariffs on members of a customs union (all of the eight except the UK and Norway) and single market (all except the UK) could be complex. In previous instances, the US targeted country-typical products (such as French wine or German cars) rather than blanket tariffs.

- **What is the legal basis?** – Which legal authority will Trump invoke? The International Emergency Economic Powers Act (IEEPA) is a likely candidate, but this could prove short-lived if the US Supreme Court rules against its use – a firm base case in prediction markets. Alternatively, the administration could rely on Section 301 (for instance, in relation to EU digital services regulation), but it is unclear how this could be targeted at specific countries. Nor would it apply to the UK.

Rapid escalation to a global trade war...?

The risk of European retaliation is high. Denmark has shown no willingness to cede Greenland, despite reports of a proposed US acquisition fund amounting to USD 700 billion. European leaders have already invested significant political capital in supporting Denmark. Public opinion across Europe is also likely to be far less tolerant of concessions than last year. In a recent ARD poll in Germany following the US intervention in Venezuela, only 15% of respondents viewed the US as a trustworthy partner – barely above the 9% recorded for Russia, and far below the 85%+ recorded for France and the UK.[1]

The EU and the UK could respond with retaliatory tariffs – with the possible activation of a EUR 93 billion tariff package from 6 February the first step – though their impact may be limited given that US exports to Europe are smaller than European exports to the US and are heavily concentrated in energy. More importantly, the EU could deploy its Anti-Coercion Instrument, designed precisely for such situations. This would allow asymmetric retaliation, for example by restricting market access for US services firms operating in Europe.

Further escalation could follow quickly. The US might raise tariffs again or, for example, curtail remaining military support for Ukraine. Europe, in turn, could rally allies worldwide to join retaliatory measures, broadening the dispute into a global trade war and materially increasing the risk of a global recession.

Or could this blow over quickly?

Following "Liberation Day" last year, Europe – as well as most other affected economies – ultimately capitulated to US demands. Fears of losing access to US markets and military support for Ukraine, alongside the desire to avoid intra-European divisions, prevented meaningful retaliation. The EU and the UK instead pledged large-scale investment in the US and reduced trade barriers, in exchange for modest tariff relief.

A similar outcome cannot be ruled out. The US may again succeed in dividing Europe: the EU's Anti-Coercion Instrument requires qualified majority voting, and countries not directly affected by tariffs could form a blocking minority. The US could also leverage Europe's security dependence. Over time, pressure could build within Europe on Denmark – and potentially Greenland – to concede.

Diverging monetary responses to potential trade shock?

If only US tariffs were implemented, the immediate economic damage would be meaningful but not overwhelming. Goods exports to the US account for roughly 3% of GDP in most of the eight affected economies; France is less exposed, at around 1-2%. A sustained shock of this kind could reduce GDP in these countries by around 0.2-0.3%. For the US, the impact would likely be negligible, based on experience to date, although weaker business confidence and thus investment cannot be ruled out.

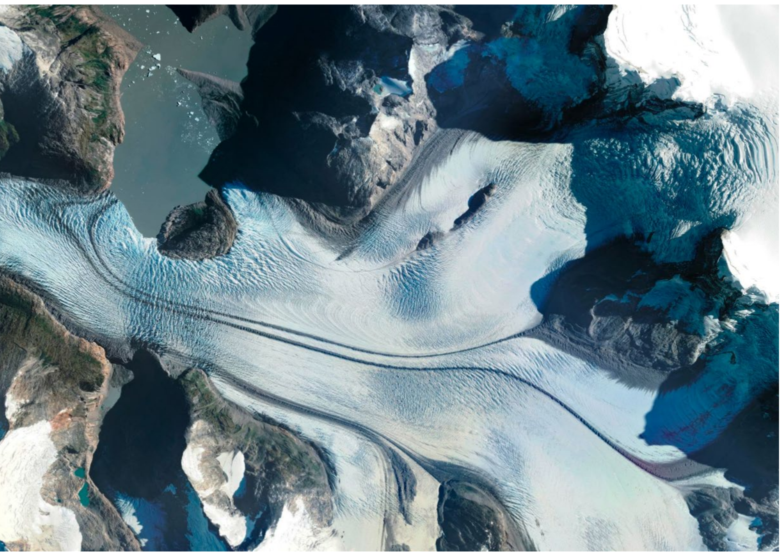
[1] As reported by Yahoo, 8 January 2026.

EU retaliation would transform the trade conflict from a supply shock for the US and a demand shock for the rest of the world into a potentially large stagflationary shock for all parties. This would materially alter the policy calculus for central banks.

For the US Federal Reserve, with inflation already above target, the risk of de-anchoring inflation expectations is arguably higher and could prevent further rate cuts. However, with its dual mandate, the Fed may put a larger weight on signs of weaker growth. So far, it has arguably looked through tariff-driven inflation and cut rates regardless. A further escalation of trade wars – especially alongside political pressure from the US administration – could strengthen the case for additional easing.

The European Central Bank, by contrast, has so far downplayed the impact of US tariffs and has even suggested that trade wars could pose upside risks to inflation, implying tighter policy. Such a response would risk exacerbating the growth shock, but it cannot be ruled out. Elevated inflation may also limit the Bank of England's room to ease.

In both the UK and the EU, fiscal stimulus may therefore become the primary stabilisation tool. Given uneven national fiscal space, the case for pan-European support financed through joint borrowing could strengthen.



Financial markets: where is the safe haven now?

Financial market reactions will be crucial. If markets remain sanguine, expecting Europe to fold, the economic cost for the US could be limited, especially as these tariffs apply "only" to Europe rather than globally, unlike last year's reciprocal measures.

Conversely, a more negative market response could pressure the US administration to soften its stance. Europeans might also find allies in the US Congress seeking to restrain presidential action and de-escalate tensions. A Supreme Court ruling against the use of IEEPA could offer temporary relief, though the administration would likely search for alternative legal routes.

- Multiple outcomes are possible, but the risk of an escalating trade war between the world's largest economies now appears significantly higher than after Liberation Day. This would likely weigh heavily on risk assets – particularly European manufacturing firms exposed to the US, and US services firms reliant on European markets.

- The euro could benefit if European investors repatriate capital from the US – which could hurt US Treasuries and thus increase pressure on the US administration as well – or in the event of any move toward joint European borrowing.

- However, neither the dollar nor the euro would likely function as reliable safe havens in this scenario, leaving precious metals – and possibly the yen – as the primary beneficiaries.

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