

## Donald Trump and the ghosts of Al Capone

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On 2<sup>nd</sup> April, in an elaborately stage-managed performance in the White House Rose Garden, President Donald Trump unveiled his long-awaited 'reciprocal tariffs' against almost every country in the world (with the conspicuous exceptions of Russia and North Korea).

On one reading, Australia escaped fairly lightly, copping the minimum tariff of 10%. China was hit with a 34% tariff (on top of the 20% already announced in the first few weeks of the Trump Administration's second term); Japan and Korea copped 24% and 25%, respectively, the European Union 20%, Vietnam 46%, Indonesia and Malaysia 32% and 24% respectively.

The harshest treatment was reserved for some of the world's poorest countries – Madagascar (with a per capita GDP in 2024 of just US\$563) will be hit with a 47% tariff (which the US embassy to Madagascar [said](#) was 'not a punitive action') on its US\$733 million of exports to the US (the largest component of which is vanilla); Laos (per capita GDP of US\$1,850) will face tariffs of 48% on its \$803 million of exports to the US; and Lesotho (per capita GDP of US\$1,062) will be on the top rung with a 50% tariff on its \$2.8 million of exports to the US. For some reason, the tiny French overseas territory of [St Pierre et Miquelon](#), which sits just off the south coast of Newfoundland, will also be copping a 50% tariff on its \$3.4 million of exports (mostly shellfish) to the US<sup>1</sup>.

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1 In the [Hotel Robert](#), on the island of Saint Pierre, there is an exhibit featuring a straw hat which purportedly belonged to the notorious gangster [Al Capone](#), who used Saint Pierre et Miquelon as a base for [smuggling liquor into the United States](#) during the Prohibition era (1919-1933), and especially after 1924, when Canada bowed to pressure from the US to curtail exports of alcohol to its southern neighbour.

Alcohol production was actually started on St Pierre et Miquelon by [Bill 'The Real' McCoy](#), after discovering that (as a French possession) it imposed much lower taxes on alcohol production than the Bahamas, which had been the original centre of this illicit trade (French authorities helpfully annulled a law prohibiting the importation of foreign sugar, molasses and rum into French colonies). At the peak of this 'trade', in 1929, over 5.8 million litres of whisky (worth some US\$60 million, or over \$850 million in today's dollars) were produced in St Pierre et Miquelon. It collapsed overnight when Prohibition was repealed in 1933. In an echo of that era, however, David Frum (a speechwriter for US President George W. Bush, who coined the phrase 'axis of evil' to describe a purported 'alliance' between North Korea, Iran and Saddam Hussein's Iraq) this week suggested that Trump's 'reciprocal tariffs' offered an opportunity for Canada to [Make Smuggling Great Again](#).

# SAUL ESLAKE

CORINNA ECONOMIC ADVISORY

Page | 2

And if the seals and penguins on [Heard and McDonald Islands](#), Australia's otherwise uninhabited territory in the Indian Ocean, dare to think of exporting anything to the United States, they will face a 10% tariff too.

The London-based magazine [The Economist](#) described Trump's announcement as "the most profound, harmful and unnecessary economic error in the modern era". The [Wall Street Journal](#)'s editorial board noted that the effective US tariff rate would now be higher than the [Smoot-Hawley Tariff](#) of 1930 which helped put the 'great' into the Great Depression, and that Trump's [new protectionist age](#) marked "the end of US economic leadership".

The way in which these 'reciprocal tariffs' were derived serves to underscore the sheer lunacy of what President Trump unveiled last week. As the [Office of the US Trade Representative](#) has spelled out, for each trading partner (including the uninhabited ones) they are calculated as the merchandise trade deficit which the US has with that counterparty, divided by the value of the US' merchandise imports from that country, and then – if that results in a number greater than the arbitrarily specified minimum of 10%, dividing that number by two, representing the '50% discount' which Trump so magnanimously offered.

So, for example, in 2024 the US ran a US\$294.5bn goods trade deficit with China, the difference between exports of \$143.5 billion and imports of \$438.9 billion. So, 295 divided by 439 is 0.67 (or 67%): divide that by two, and hey presto the tariff on imports from China is 33.5% rounded to 34% (plus the 20% that already applied).

For Australia, that calculation ought to have been, according to the [USTR Office](#), US goods exports to Australia of US\$34.6 billion minus imports from Australia of \$16.7 billion, giving a *surplus* of \$17.9 billion: divide that number by 16.7 and the tariff on US imports from Australia should have been *minus* 107%! (ie, in effect, a subsidy).

Because, by the logic (if that's what it can be called) behind these calculations, that's the measure of the extent to which the US has been 'cheating' in its bilateral trade with Australia.

Of course, neither Australia nor any of the other handful of countries with which the US runs a merchandise trade surplus will be getting a 'subsidy'. We don't even get a '50% discount'! We just get the arbitrary minimum of 10%.

In thinking about what all this means for Australia, it's important to remember that – contrary to what Donald Trump and those around him think and say – those tariffs will be paid primarily by American consumers, not by Chinese, Canadian, Mexican, Australian or any other exporters to the United States. And, what's more, they know it – which is why over the two months since Trump's inauguration, longer-term US household inflation

# SAUL ESLAKE

CORINNA ECONOMIC ADVISORY

Page | 3

expectations have risen to their highest level in 41 years. That will deeply concern the US Federal Reserve, America's central bank, because history tells central bankers that if people (and businesses) *expect* inflation to remain high, they will behave in ways that make it more likely that it *will* remain high – for example, by putting up prices to claw back cost increases which they expect to occur in the year ahead, not just those which they have actually experienced over the past twelve months.

The direct impact of the 10% tariffs on imports from Australia will be relatively small – chiefly because the US in recent years has typically accounted for less than 5% of our total exports of goods. Moreover, two of our most important exports to the US – gold (exports of which have surged to such an extent in the first two months of this year that Australia has actually run a surplus with the US for the first time since the Korean War wool boom of 1951-52) and pharmaceuticals – will apparently be exempted from the tariff, at least for the time being.

The products most likely to be adversely affected are beef (which is Australia's largest single export to the US, and for which the US is our largest market) and other meat, principally lamb (which is Australia's fourth-largest export to the US).

Hopefully, beef exporters will be able to find alternative markets for whatever they're not able to sell to the US, as they did when faced with punitive tariffs imposed by China earlier this decade (although unlike in that episode, they will be facing competition from other beef exporters, such as Brazil, who are also subject to 'reciprocal tariffs'). If beef producers aren't able to find alternative markets, the result will likely be cheaper meat for Australian consumers at butchers' and supermarkets.

The greater concern for Australia is the *indirect* effects of the tariffs, via their impact on trading partners which are much more important to Australia than the US – in particular China (which accounts for around 35% of our total goods exports), but also Japan (a little over 13%), Korea (7½%), and South-East Asia (over 12%). The tariffs which the US has imposed on imports from these countries are explicitly intended to discourage imports from those countries, with whom the US runs large bilateral trade deficits. To the extent that they succeed in that aim (which is debatable), those countries will likely import less iron ore, coal, LNG and other products from Australia which are inputs into the products which they in turn export to the United States.

That will result in lower prices for those commodities – which is why the Australian dollar fell so sharply in the aftermath of Trump's announcements, despite the US dollar also weakening further – as well as a lower volume of exports.

This is why the Treasury has [estimated](#) that the *indirect* effects of Trump's tariffs on the Australian economy will be nearly four times as large as the *direct* effects.

# SAUL ESLAKE

CORINNA ECONOMIC ADVISORY

Page | 4

The effects on Australia would be worse if the Australian Government were to follow other countries (including China) in ['retaliating'](#) against Trump's tariffs by imposing tariffs on imports from the United States.

['Tit for tat' retaliation](#) is [circular firing squad](#) stuff: it simply doesn't make sense to force Australian businesses and consumers to pay higher prices for things imported from the Americans, just because the US Government wants to force American businesses and consumers to pay higher prices for everything imported, from everywhere else in the world, into the United States.

That's especially so when you consider that Australia imports more than twice as much stuff from the US as we export to it. 'Retaliation' would mean Qantas and Virgin would be paying higher prices for their new Boeings (so we'd all be paying higher air fares); farmers would be paying higher prices for their green-and-yellow tractors and harvesters (so we'd be paying higher prices for the food they produce – or more likely, farmers would have lower incomes); trucking companies would be paying higher prices for trucks (so we'd be paying higher prices for the things carried in them); and we'd be paying higher prices for cosmetics, pharmaceuticals and a range of other items we import from the US.

The Morrison Government, sensibly, didn't respond to China's imposition of extortionate tariffs on imports of Australian barley, wine, meat, seafoods and coal earlier this decade by forcing Australian consumers to pay more for all the stuff we import from China – and, thankfully, it seems probable that the Albanese Government's response to the tariffs imposed by the Trump regime in the United States will be similarly measured and sensible.

It's also to be hoped that the Government will not succumb to pressure from Australian industries to force other Australian businesses and Australian consumers to pay higher prices for products that might be diverted to Australia (among other countries) which can no longer be exported to the United States by imposing so-called 'anti-dumping' duties (ie, tariffs) in response to every request for them.

But with it now seeming [increasingly probable](#) that the US economy will be pushed into a (completely self-inflicted) recession – and with other countries, including in particular China, less well-placed to ward that off than they were at the time of the global financial crisis (in part because of the huge amounts of debt which they ran up responding to that episode and to the Covid-19 pandemic) – there is a growing risk that Australia, too, could be faced with a more protracted economic slowdown or even recession. And if that were to be combined with more persistent inflation, the capacity of the Reserve Bank to ameliorate that risk by cutting interest rates would become more complicated.

# SAUL ESLAKE

CORINNA ECONOMIC ADVISORY

Page | 5

More broadly, Australians, and in particular our political leaders – like their counterparts in Canada, Europe, Japan, South Korea, Singapore and New Zealand – need to be thinking clearly and coherently about the implications of a world in which the United States is neither a reliable and trustworthy trading and security partner or indeed even a 'friend', as it has been since mid-way through World War II.

Australia is not merely [one of a minority of countries with which the United States runs trade surpluses](#) (in fact it runs larger trade surpluses with only three other economies – the Netherlands, Hong Kong and Singapore – than it does with Australia). It is the only nation whose military has fought alongside Americans in every military conflict that the United States has been involved in since 1917. It hosts crucial (to the US) [military bases and intelligence-gathering facilities](#) which, some say, would be [nuclear weapons targets](#) in the event of a conflict between the United States and an adversary with nuclear weapons capabilities. And we are now in effect giving the US [foreign aid](#) as part of the AUKUS agreement, the first US\$500 million (of what will ultimately be US\$3 billion) Defence Minister Richard Marles took with him on his visit to Washington DC in February.

Yet all of that counts for naught with the Trump regime. And in that context, it is important to remember that Donald Trump is back in the White House because a plurality of the American people elected to put him there, in the full knowledge that he would do what he did last week. Which is why it is so important for Australians, and the people of America's other traditional friends and allies, to understand that the American people have themselves changed. And so, therefore, must we.

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