Trade and US tariffs: Explainer and lessons for Australia

Alan Duncan, Abebe Hailemariam and Daniel Kiely

Key insights

- Despite claims to the contrary, the US Liberation Day tariffs are not 'reciprocal'.
- The risks to Australia from US tariffs are as much indirect as direct, via their impacts on global markets and the economies of our regional trading partners.
- Australia's trade with China was worth $2,600 per Australian household in 2022-23, and lowered prices by 4 per cent.
- Australia's strategy of protecting fair trade while diversifying export markets should drive payoffs in the longer term.
- There are good prospects for beef exporters to pivot to new markets on the back of US tariffs. But Australia needs to be proactive in the face of competition from Brazil as an alternative supplier of displaced trade.
- Financial markets have priced in rate cuts from the RBA in response to an expected slowdown in global economic activity from the US tariff cuts.

Introduction

Ever since Adam Smith published The Wealth of Nations in 1776, economic theory and empirical evidence show clear gains from trade based on specialisation.

And yet the United States has ripped up 250 years of trade theory in the past few months with the precipitous actions of US President Donald Trump to penalise countries who run an overall trade surplus with the US.

Through the imposition of trade tariffs, the US administration has fundamentally disrupted the global economic landscape, posing new challenges to economies around the world, including Australia.

The almost daily announcements of new, reduced or deferred tariffs[1] have introduced massive uncertainties for governments, central banks, businesses and investors.

This note looks to explain the economic basis for tariffs, the apparent motives and impact of the so-called 'Liberation Day' tariffs, the benefits of trade, the exposure of the Australian economy to tariff wars, as well as discussing potential responses from an Australian perspective.

What are tariffs and how might they be used?

Tariffs are taxes imposed on imported goods paid to the government by the importing (domestic) company.

Tariffs almost inevitably lead to an increase in domestic prices as importers pass at least some of the tax onto consumers.

And as prices in the importing country increase, this means that, other things remaining equal, there will be less domestic demand for exports from those countries that are subject to the tariff.

Exporters may consider lowering the prices they charge to importers (reducing margins) to minimise the impact of the tariff on the demand for their goods. But this depends on whether trade remains economically viable from the exporter's perspective.

Another response is for exporters, where possible, to switch to alternative export markets that offer more favourable terms of trade.[2] And governments may themselves impose reciprocal tariffs on imports in response to tariffs on their exports.[3]

Others may do so to protect domestic industry from overseas competition. There may be justifications for such. For example, if other countries heavily subsidise an industry, it may make the global market

[1] On 10 April 2025, 8 days after the Liberation Day tariffs were introduced, a 90-day deferral of so-called 'reciprocal' trade tariffs was announced.

[2] As a formal economics definition, the *terms of trade* between countries are dictated by the ratio of an index of export prices to an index of import prices – either for specific commodity groups, or an overall price index. Import and export prices, and hence the terms of trade, take account of tariffs imposed by either party.

[3] Tariffs have the effect of tilting the terms of trade towards the country imposing an import tariff, and reciprocal tariffs (including those tariffs that are retaliatory in the genuine sense of the term) act to rebalance those terms back towards the exporting country.

uncompetitive, and tariffs may be seen as an instrument to level the playing field.

Sometimes tariffs are introduced to counter other non-tariff trade barriers on a country's exports, such as import bans, quotas or restrictive administrative barriers. Or imports to a nation may be deemed as 'dumping' – with prices set below cost price to drive out domestic competition.

Ultimately, tariffs are among the key instruments for protectionism.[4]

The Liberation Day tariffs

On 2 April 2025, the Trump administration announced a universal baseline tariff rate of at least 10% on goods imported to the US from around 90 countries, with specific import tariffs reaching as high as 50% for some countries.

The US subsequently granted (on 9 April 2025) a 90-day reprieve on specific bilateral tariffs to all countries bar China, reverting to the universal 10% baseline (at time of writing). The ostensible reason for the tariff pause was to facilitate trade negotiations with those countries.

China was singled out as an exception to the 90-day reprieve granted to other countries, with the tariff on Chinese imports later raised by the US to 145% in response to China's own retaliatory actions.

President Trump claims that these measures will reduce the US trade deficit, boost the economy and protect jobs.

Reciprocal
adjective [ri-sip-ruh-kuhl]
From Latin reciprocus (based on re- 'back' + pro- 'forward')

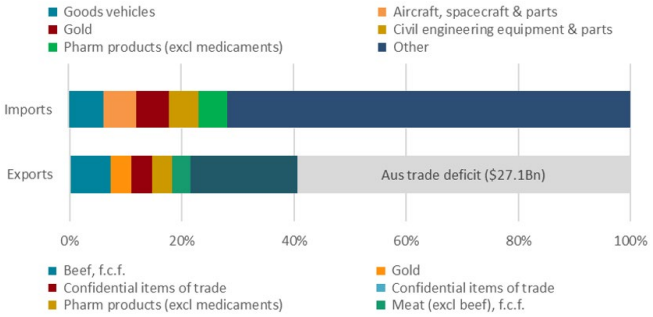
1. relating to an action done in response to another action in a way that is equivalent to it.
2. involving two people or groups who agree to help each other by behaving in the same way or by giving each other similar advantages.
3. operating for two parties, especially equally or to a similar degree.

So, how were these tariffs calculated?

Contrary to being 'reciprocal' in nature, the formula released by the United States Trade Representative (USTR) shows that the tariff on a trading partner is calculated simply as half of the US trade deficit (exports minus imports) divided by imports from the respective country.

For countries where the US has a trade surplus, like Australia (see Figure 1), a universal 10% tariff was levied for most products imported to the US.

Figure 1: *Australia's goods trade balance with US, 2023-24*



Source: Bankwest Curtin Economics Centre | based on DFTA Australia's Goods and services by top 15 partners 2023-24.

This is not a reciprocal tariff.

Beyond the generic trade surplus formula, no further country-specific factors were considered in the level of tariffs imposed by the US. And specially, the tariff levels have nothing to do with whether other countries have in fact imposed a tariff on US exports.

The application is also inconsistent.

Other non-retaliatory justifications were given for imposing tariffs on Australia, with claims that the Australian government banned US beef imports, or maintained burdensome administrative processes that affected US pharmaceutical exports.

Trade restrictions were imposed by Australia, but they related to bio-security measures to protect against the likes of mad-cow disease.

[4] Non-tariff trade barriers constitute other forms of trade controls including quotas, safety regulations, trade embargos, among others.

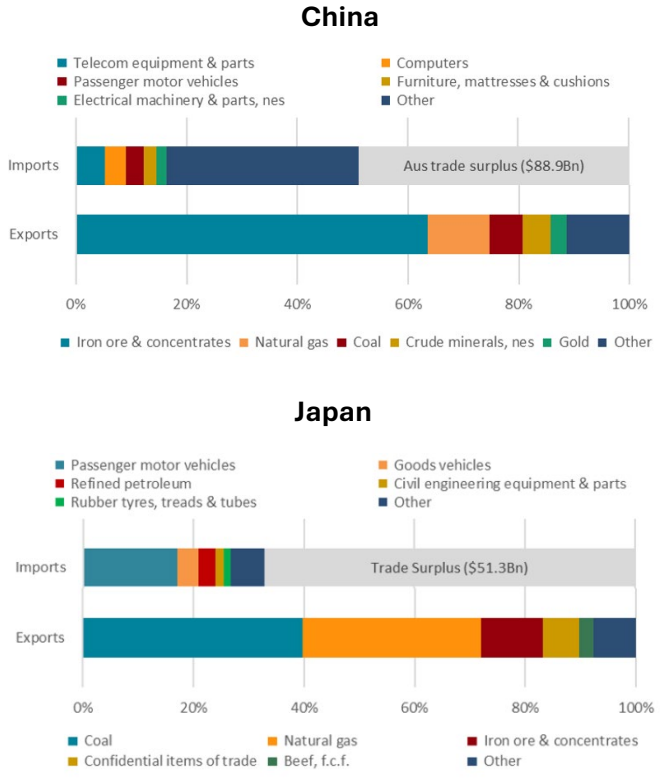
This is unexceptional as a rationale for imposing trade conditions, in the same way that any other jurisdiction would be entitled to use fiscal policies to support access to medical treatments and medicinal health.

It is not reasonable to think that a trade deficit should *de facto* lead to the imposition of a tariff, any more than it would for Australia to impose such a tariff on the US based on the nation's trade deficit.

Neither would it be reasonable for other countries with which Australia runs a trade surplus to raise tariffs purely on that basis.

For example, despite the import of many Chinese-manufactured goods, the scale of Australian exports of iron ore to China leads to Australia running a large trade surplus (Figure 2). Australia also runs a trade surplus with Japan, primarily driven by Australian exports of coal and gas.

Figure 2: *Australia's trade balance in goods with China and Japan, 2023-24*



Source: Bankwest Curtin Economics Centre | based on DFTA Australia's Goods and services by top 15 partners 2023-24.

But would it serve China's economic interests to impose tariffs on Australian exports purely on this basis?

The answer is no.

To do so would increase the price of iron ore and in turn inflate steel, construction and other related downstream prices. This would hit China's economic growth.

Are Trump's tariffs logical?

In a stylised world, imposing a tariff on imports raises domestic costs and reduces competition for domestic producers. This may lead to higher prices to the extent that costs are passed onto consumers.

Import tariffs could expand domestic production in the longer term and increase profits, depending on the responses of consumers to any change in prices. The government may also get some boost to the revenues collected through tariffs.

But, in a complex and interconnected global economy, the disruptions faced by domestic industries are likely to be larger than any potential gains.

Take a tariff on aluminium imports as an example. This will drive up the price of locally manufactured cans for beverages. Larger producers may be able to absorb higher input costs or negotiate lower prices.

Some may be able to substitute to alternative inputs – such as using glass bottles. But the fact they were not doing this already suggests that the market did not want such, or it was less efficient to do so.

Smaller firms, such as micro-breweries, have less ability to negotiate, and lack the capital to switch inputs, change production processes, or reskill workers to new process techniques.

And tariffs cannot be a long-term solution to reduce trade deficit in a world with minimal restrictions of capital flows and independent monetary policies.

Ultimately, consumers will be penalised through less choice and increased prices.

Lessons from the Great Depression

Some have likened the US tariffs to the **1930 Smoot-Hawley Tariff Act**, signed by President Hoover with the aim to shield US industry from the Great Depression.

The Smoot-Hawley Act imposed a 20% tax on imports to the US, against the advice of senior economists at the time, and led to retaliations from trade partners. The Act has since been tagged as one of the major contributors to exacerbating the Great Depression, by restraining business recovery, escalating unemployment and inflating prices for households.

Developed economies learned from this.

The Bretton Woods-General Agreement on Tariffs and Trade (GATT) came into play at the end of World War Two, establishing new rules for post-war international economic ties between allied nations.

This led to the creation of the International Monetary Fund (IMF) and the World Bank, which have – until now at least - remained cornerstones of economic development and growth. More recently (in 1995), the World Trade Organisation (WTO) was established with a mandate to remove trade barriers and enhance free trade.

The benefits of free trade for Australia

So, what are the benefits of Australia's trade with China and other nations? Increased trade flows, more employment, higher incomes and lower cost-of-living effects are key benefits.

Trade flows and investment

The Australia-United States Free Trade Agreement (AUSFTA) went live in January 2005. According to DFAT, "*since AUSFTA came into force in 2005, bilateral goods and services trade between Australia and the United States has more than doubled, and two-way investment has more than tripled*."[5]

BCEC's Trading Up report[6] estimated that since FTAs came into force Australian exports to China have increased by $275.4 billion (bn), exports to Japan by $99.1bn, and exports to Korea by $40.7bn, with exports to Thailand increasing by $57bn.

Household income

BCEC estimated that the total amount of real household disposable income attributed to overall two-way trade in 2022 was $16,200 per household and $6,400 per person in Western Australia (WA). On aggregate, this translates to $17.9bn for WA households in 2022 alone.

A major concern for Australia from US tariffs is the indirect impact via this key export market. Any slowdown in China will affect demand for Australia's exports.

BCEC's analysis of Australia's trade with China estimates that two-way trade increased disposable income by an average of $2,600 per Australian household in the 2022-23 financial year, reaching as high as $8,700 in some states.

This equates to 4.6% of disposable income per capita and $29bn on aggregate to Australian households.

Employment

In terms of contributions to employment, BCEC findings show that trade with China supported around 595,600 jobs in Australia, accounting for 4.2% of the nation's total employment in 2022-23.

A global or Chinese economic slowdown will not turn income and employment gains to zero. But it is important to know the size of the overall China-Australia trade benefit at the household level.

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[5] https://www.dfat.gov.au/trade/agreements/in-force/ausfta/australia-united-states-fta#:~:text=The%20United%20States%20is%20the,at%20%241.20%20trillion%20in%202023.

[6] Buckland, A., Duncan, A., Farhad, M., Hailemariam, A., Kiely, D., Sanchez Arenas, V., and Sotirakopoulos, P., "Trading up: International trade futures and the Western Australian economy", Bankwest Curtin Economics Centre, Focus on Industry Report Series, No. 8, July 2023.

Consumer choice and inflation

Trade also brings welfare benefits to households. In addition to providing consumers with greater choice, imports can help to control inflation.

Over time, the price of tradable items has increased at a far lower rate than that of non-tradable items across Australia. The price of tradable items did increase sharply during the pandemic because of border closures and supply chain constraints.

But the stabilisation of CPI in tradables has been an important factor in getting inflation back to within the RBA's target range .

BCEC modelling[7] showed that Australian households would face an average 4.2% rise in expenses if they were forced to consume products from economies outside of Australia's primary trading partners.

To the extent that US tariffs might force a shift in Australia's trade to more expensive trading partners, this could add to the cost-of-living pressures being faced in Australia.

The RBA is more likely to drop the cash rate as response to any slowdown in global economic activity. Mortgage holders may get some benefit from reduced repayment rates, but this assumes that employment and wages remain steady – not something that can be taken as given.

Potential impacts of tariffs on the Australian economy: direct exposure

The direct effects on Australia from the Liberation Day tariffs will most affect those industries that directly trade with the US.

So, what are the key products traded between the two nations?

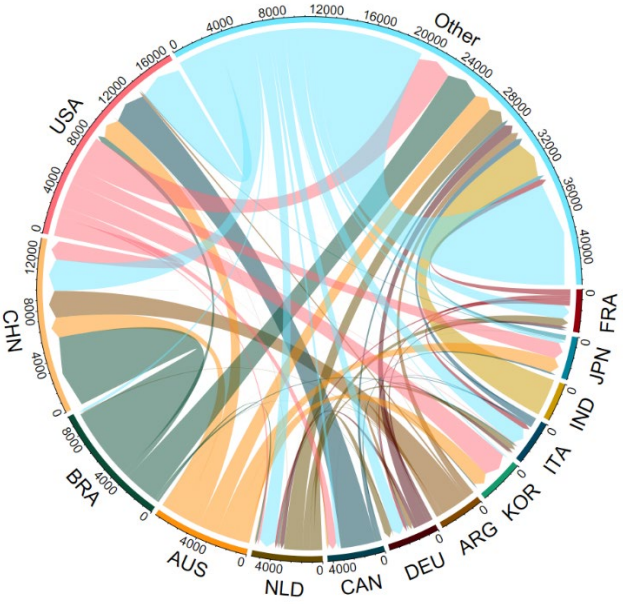
Australia imports far more from the US than it exports to the US, with an import value of $88.2bn compared to exports valued at $37.5bn in 2023-24. The main imports from the US include passenger motor vehicles, aircraft and space parts, goods vehicles, pharmaceuticals and medicines.

The US is a major market for Australian beef and other meats, with exports in 2023-24 valued at $3.3bn and $1.5bn respectively.

The imposition of a 10% tariff on Australian beef and meat exports could have significant implications for those industries. But there could also be opportunities to offset some of the effects, with an eye on building more reliable and sustainable longer-term markets.

Figure 3 shows the global trade flows in beef, and a couple of flows are worth pointing out.

Figure 3: *Global trade in beef*



Note: Based on 2023 data.

Source: Bankwest Curtin Economics Centre | From Gaulier, G. and Zignago, S. (2010) BACI: International Trade Database at the Product-Level. The 1994-2007 Version. CEPII Working Paper, N°2010-23.

First, Australian beef imports are negligible ($16m from NZ makes up 70% of imported beef in 2023-24). So, Australia's need to import beef is limited. Neither are any bio-security measures solely targeted at the US.

Second, while the US remains a key market for beef exports from Australia, other growth markets with China, Korea and Japan are very much in play.

[7] Ibid

Thirdly, Korea, Japan, Canada and China are all key markets for US beef exports. Any deterioration in trade with these economies may open new opportunities for Australian producers, noting that the demands and willingness to pay for 'like-for-like' beef products may differ across markets.

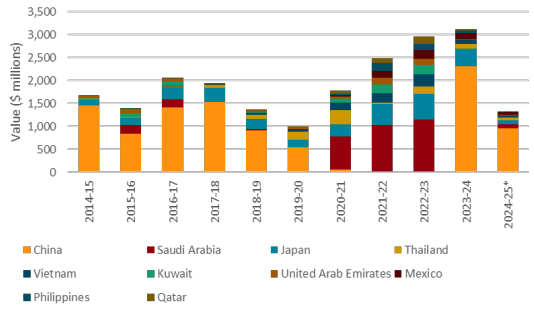
But Australia needs to be on the front foot and proactive. Brazil is in a strong position to strengthen its connections to markets in Europe and Asia, and China is actively courting Brazil as an alternative supplier as it looks to shift away from US beef exports.

Chinese tariffs on Australian exports – what have we learnt?

During COVID-19, another event occurred that impacted the world of trade. China introduced several tariffs and embargos on Australian exports. Tariffs were imposed on barley, wine, and coal, as well as lobsters, lumber, and several other goods.

These tariffs affected the make-up of Australia's exports, with a heavy substitution of export volumes away from China towards other markets.

Figure 4: *Australia's barley exports*



Note: *2024-25 is from July to January 2025. Caution is needed with monthly data due to confidential commodities, which can be more easily addressed over a full FY.

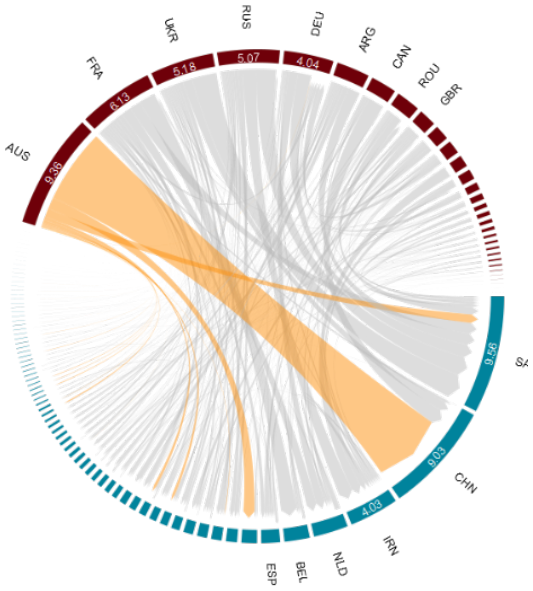
Source: Bankwest Curtin Economics Centre | based on DFTA Country SITC Pivot Table.

Barley exports quickly pivoted to other markets including Saudi Arabia, Japan, and other Middle East and Southeast Asian countries.

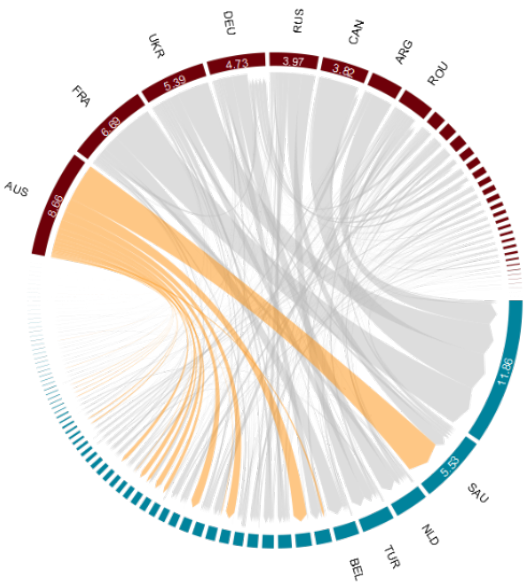
And Saudi Arabia emerged as the largest buyer, taking over about two-fifth of Australia's barley exports in 2020-21.

Figure 5: *Global trade of Barley, quantity in tons, by country, 2017 and 2021*

2017



2021



Source: Buckland, A., et. al., 2023.

At the same time, China expanded its trade relationships with other barley exporters in Australia's place, with France, Canada, and Ukraine being the major partners of choice.

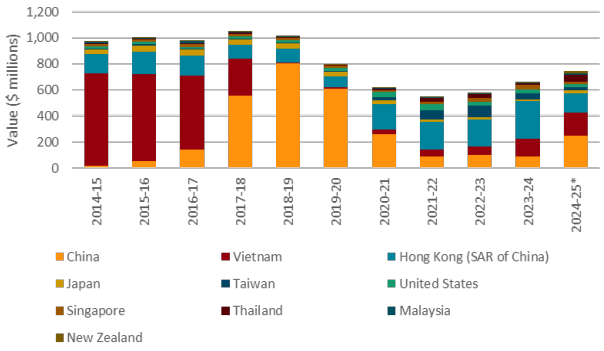
With the recent removal by China of tariffs on Australia barley, we have now seen a re-pivot of Australia's exports back to China.

This again emphasises the importance of looking at long-term relationships and not burning bridges with short-run or overtly retaliatory tariff measures.

Other goods, such as crustaceans, faced a more difficult path. Many businesses were forced to pivot to the frozen food market for a higher share of their exports, which attract lower prices.

For example, the value of crustacean exports from Western Australia fell by 41.2% from 2019 to 2020, and a further 30% from 2020 to 2021, with the industry shifting to new partners to meet allowed quotas.

Figure 6: *Australia's crustaceans exports*



Note: *2024-25 is from July to January 2025. Caution is needed with monthly data due to confidential commodities, which can be more easily addressed over a full FY.

Source: Bankwest Curtin Economics Centre | based on DFTA Country SITC Pivot Table.

During the same period, the industry also had to deal with skyrocketing freight costs during the fallout from the pandemic to the point where the state governments needed to intervene and partially subsidise the costs of air freight for crustacean exporters.

Such supports helped many businesses stay afloat.

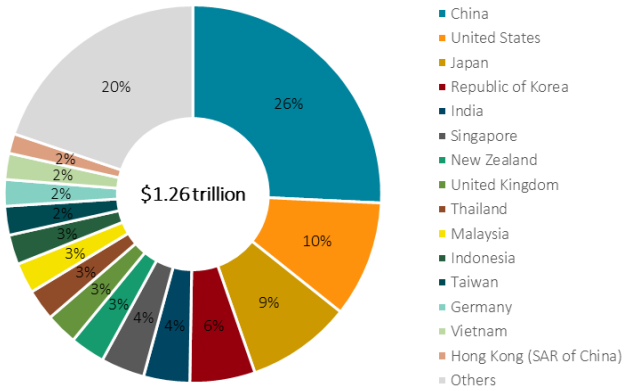
Australia's exposure to international trade: indirect exposure

The imposition of US tariffs on Australia's key trading partners poses a larger risk than the direct effects of the import tariff on Australian goods to our domestic economy.

And as our major export partner, any slowdown in the Chinese economy poses a particular risk to demand for iron ore and exports of high-quality agricultural produce.

As of 2023-24 about 80% of Australia's two-way trade in goods and services (defined as imports plus exports) sits with 15 trading partners. In fact, the top five account for a half of Australia's overall two-way trade.

Figure 7: Australian two-way trade, 2023-24



Note: Top 15 and others.

Source: Bankwest Curtin Economics Centre | based on DFTA Country SITC Pivot Table.

China tops the list at 26% ($325.5bn), with the US the second largest trading partner at 10% ($125.8bn) of total two-way trade – mainly from US imports as noted earlier.

Japan is in third place at 9% ($113.4bn), followed by Korea as the fourth largest trade partner. Many other economies sit at between 2 to 4% of Australia's trade.

Australia has seen growth in trade with most of these economies over the last five years, with 17% growth for Taiwan, 16% for Korea and 15% for Vietnam. There has also been strong trade growth between Australia and India, up 14% over a five-year period.

Such trade diversification is certainly encouraging, with Australian businesses picking up opportunities presented by FTAs and the expansion of the middle classes in many developing Asian economies.

Past booms in commodity markets including iron ore, coal, and liquified natural gas has bolstered Australia's economic growth.

These commodities have consistently contributed to Australia's trade surplus with key Asian trading partners, despite fluctuations in global market conditions.

Agricultural products such as beef, wheat, and other meats account for a significant share of Australia's export portfolio and play a key role in boosting the domestic economy. Australia's high quality and strong agricultural brand amidst the evolving demand for high quality food products by international consumers, needs to be upheld.

Australia has managed to avoid recessions during previous global crises such as the GFC and COVID-19 pandemic.

Good fiscal policy coupled with a large and strong Chinese economy were key to this. The extinct to which China avoids recession in this new world of trade remains to be seen. But this will be critical to Australia's longer term economic footing during these increasingly uncertain economic conditions.

Summary and policy discussion

International trade is at the heart of the Australian economy, contributing to economic growth and job creation.

The rise in global protectionism following Trump's tariff creates downside risks for Australia that necessitate well-designed and coordinated responses.

Protectionist strategies are not the solution. Free trade is critical to economic growth, generating employment, income, and lower costs of living as well as greater consumer choice.

The Federal government must continue to secure FTAs and maintain positive economic ties with key trading partners, particularly as they relate to the nation's position in the Indian Ocean.

Businesses need to explore opportunities in other new markets. This includes access to inputs across their supply chain as well as new opportunities for export markets to minimise exposure to global trade shocks.

Together with the enablers provided by government, business must look to upskill workers and technological capabilities to ensure that production processes and products are positioned to be at the forefront of global innovation and seize any new market openings that emerge because of trade wars.

Government proposals in response to the Trump tariffs include providing $50 billion funding support and zero interest loans for affected industries, as well as strengthening anti-dumping laws. Such responses are to be welcomed.

Commitment to the defence of fair trade practices while simultaneously diversifying export markets will pay-off in the long-term.

But there is also a strong imperative to address the broader implications of rising protectionism and formulate effective strategies to mitigate the potential adverse effects.