

Chris Burrell's Market View Blog

Black Swan: Trump Tariffs

A “black swan event” is a metaphor, popularized by Nassim Taleb, describing a rare, unpredictable and impactful event. These events, once they occur, have a profound and often disruptive impact on society, economics or specific industries. There is a hindsight bias, in that people tend to look back and find reasons or explanations for why the event was predictable, even though it was not. Examples include: the 2008 financial crisis, Covid-19 pandemic, the terrorist attacks on September 11, 2001 and the discovery of black swans in WA, which challenged the previously held belief that all swans were white.

On Monday 31 March 2025 as the markets were closing the March quarter, your diarist dictated a blog. Markets had corrected being line ball for the nine months year to date. On average Burrell portfolios had held well, not experiencing the falls of portfolios with higher growth stocks and with the fixed interest and property weightings acting as stabilisers. It was in those higher growth stocks that the corrections had occurred.

Tariffs were announced by Trump in respect of motor vehicles and Canada/Mexico. With respect to Canada/Mexico, there had been some sensible correction such that goods subject to the North American treaty (NAFTA) covering Canada, US and Mexico would be exempt. The more sensible approach on NAFTA gave cause for a view that the coming reciprocal tariffs on April 2 would also be measured.

At 4 PM Wednesday April 2, Trump presented his “reciprocal” tariffs after the markets had closed in the US Rose garden. These tariffs are not reciprocal. The tariffs were presented as such by Trump in a well-oiled marketing spiel, which included many of the platitudes oft espoused. It was only when a table was produced of tariffs by country that concerns mounted Australia was shown as having a 10% tariff. That was a bit of a shock, as under our free trade agreement with the USA, there are almost no tariffs on US goods entering Australia. There had been concern that the US administration may include the Australian GST of 10% in their calculations. The folly of this calculation had been

pointed out to the US administration on a number of occasions. Similar to the VAT in Europe (EU), such GST and VAT are calculated on all goods imported or otherwise, and so do not amount to a discriminatory tariff. The US has retail sales taxes at the State level, which are equivalent, but conveniently ignored by Trump. During the speech there was also mention by Trump of Australian beef. Again this is a furphy. The US beef herd is at relatively low levels and Australian beef is primarily used for blending in the production of hamburgers. It is a necessary ingredient by the US burger chains to provide US consumers with cost-effective beef.

The table of proposed tariffs included some high numbers such as 67% for China and 90% for Vietnam. Even the European Union was shown at 39%. Trump was proposing to discount these tariffs by half, so that China was 34%, Vietnam 46% and the EU 20%. It wasn't until later in the day, Thursday local time, that it became clear that the "reciprocal" tariffs were a fraud. The way they were calculated was not to see the level of tariffs imposed by a country on the USA, which in the case of Australia would be close to zero. Rather, the US administration had taken the trade deficit between the US and each country, divided it by the exports from the foreign country to the US and that was the number showing as the gross, to which the 50% tariff applied. This fraudulent calculation triggered an immediate global reaction, as it was seen to upend the rules of global trade, which have applied since 1947.

Some years ago your diarist was on a ship that sailed through the Panama Canal to New Orleans. Aboard was the CEO of the Port of Tampa. He had previously been TIC of the Panama Canal during the handover from the US to Panama. He was a learned presenter. It was pointed out in his lectures that the world's standard of living had gone up in lock step with the increase in global trade. It was the freeing up of global trade in accord with the economic principle of comparative advantage that had allowed our standard of living to continuously improve since World War II. In the previous blog, it was commented that Trump does not understand the law of comparative advantage.

The rose garden announcement and the fraud of the calculations presented constitute a major error by the US administration of catastrophic proportions. This is a Black Swan event i.e. an event from left field, which, while there was some risk known prior to the event, the actual outcome is catastrophically more negative than was anticipated. Global markets started to react. The reaction increased as Trump's lieutenants espoused the virtues of the Trump tariff announcements, threatened countries not to retaliate and invited countries to pay homage on a country by country basis by visiting Washington. The next day the same pitch from the lieutenants only made matters worse. Canada retaliated on the 25% car tariffs, but having been excluded from the Table, took no further action. China issued an order that there would be no further investment in the US. The EU requested the same of its businesses. China then issued a retaliatory tariff of 34% on all goods from the USA. This was to be predicted from China in so far as Chinese exports to the USA are only 15% of its total exports which in turn are only 20% of Chinese GDP. However, China has significant interests in Vietnam and other Asian countries which are affected by those tariffs. Global markets continued their meltdown on Friday, culminating in further dramatic falls of around 6% to close out the week.

There is no easy resolution to this matter. The greatest strength of the USA is that it is myopic, but that is also its greatest weakness. The US did this to us with the global financial crisis (GFC). It was reasonable for the rest of the world to think that the US had their mortgage market under control. What was discovered was a fraudulent and hopelessly managed mortgage market, which all but collapsed. The Trump tariffs are in a similar vein, in that the US president does not understand global trade, does not understand tariffs and purports not to care. The fact is this is a personal vendetta of a view that he has carried for decades. That means it is unlikely there will be a quick turnaround. Things may well get worse before they get better. The EU is considering a dramatic response. The USA has transitioned from a goods to a services economy. This is consistent with developed economies, including Australia. The services sector gets larger. It is better for the USA to have exports such as Microsoft cloud, Google search and Accenture consulting services, whilst the lower value goods, such as sneakers and clothing are produced in Asia. If the US consumer thinks about it, with their economy at close to full employment, they're probably quite happy to have a higher paid services job, than to be in a factory making sneakers and low value clothing. The EU constitutes some 450M people, compared to around 347M for the USA. It is likely that France and Germany will retaliate with a robust response, including services. It is also likely they will charge the USA with breaches of the world trade organisation (WTO) principles and will seek to exact punishments for these breaches. China has already advised they will be referring the USA to the WTO. In short, escalation is likely over the next period, rather than a turnaround from the US.

There is no easy fix in terms of the US legislative structure. The US Constitution is framed on the basis that the House of Representatives and the Senate may pass legislation, and once legislation is passed by both houses, it is sent to the president. The president has a right of veto if he does not agree with those bills. The role of the president and the executive is set down as being to administer the laws passed by the Congress. Over time, the Congress has given to the President by legislation, emergency and other powers, which allow the president to impose tariffs by executive order. Some of these powers are emergency powers in wartime, and so there is some constitutional query with respect to these tariffs. To begin with, the so-called fentanyl tariffs were announced as an emergency measure to stop the flow of fentanyl and immigrants across the borders from Mexico and Canada to the USA. It is unlikely that this was ever true of the Canadian border. However, generally the US courts have taken the view that if the President says these are an emergency measure, they will not look behind that pronouncement.

The US Senate passed a bill two days ago providing that there should be no tariffs on Canada. The Democrat minority in the Senate was supported by four Republican senators for the bill to pass. That bill must now go to the US House of Representatives, where the Republicans hold a majority of six i.e. 221 to 215. Thus if four Republicans who understood economics decided to support the bill, it would be passed. However, as soon as it arrives on the President's desk, he will apply his veto. To negate a veto requires a 2/3 majority vote of both houses of the US Congress. This will not happen any time soon stop. This is not a solution.

There is some light in the US courts considering the tariff table and whether such is authorised by existing legislation. It is in fact not an emergency and the basis of calculation is fraudulent. Might the US Supreme Court, even though stacked with Trump nominees, take the view that such a table is not valid unless passed by the US Congress?

So where to from here? On the scenario set out above, it seems that we may be in for a period of disruption until there is some reversal or negotiation of these tariffs. There will be significant pressure on the US administration from US business and within the US Republican party as many will understand the dangers of what has been announced. It is only 18 months until half of the House of Representatives are due for re-election, as that happens every two years. There will be Republican Congress men and women concerned about their prospects of re-election, given the events of recent days. There will also be a number of countries, including Vietnam, who have asked for a pause in the tariff and for negotiations to commence. They have already dispatched a trade envoy to the USA. The Vietnamese government have spoken to Trump and indicated they would be prepared to remove all tariffs to the USA in return for the US taking the same action. There is a suspicion that the Trump administration see 10% as the permanent minimum tariff, with such funds being used to contribute towards the US military globally, to providing tax cuts and for repayment of the US debt. It may be that a 10% tariff would be seen by markets as something that could be lived with for the next 18 months.

So we have a Black Swan event, which may be reversed or ameliorated at any time. This makes it difficult to set out a course of action in terms of portfolios. The dramatic falls on Thursday and Friday last have already provided attractive buying opportunities in overseas markets. But the prognosis to resolve the matter is not good. Some will take the view that until there is an announced reversal of the tariffs or amelioration of the tariffs, that the market will not bottom or show capitulation. On this basis many will sit and watch until there is greater clarity before making additional investments.

In terms of selling, the Australian reaction was relatively muted. The tariffs are an act of self-harm to the USA primarily. The evidence from the Trump tariffs in the first presidency was that prices in the USA simply increased by exactly the amount of the tariff. This does not particularly impact on Australia in the first instance as our level of exports to the USA is not material to the Australian economy. Australia, though, is not immune from a global recession, with JP Morgan increasing the probability to 60%. It is the second order effects of the Trump tariffs around the world as consumers sit on their hands and do nothing and businesses cease investment. Were these tariffs to remain and the matter not to be reversed or negotiated to an acceptable level for a considerable period, the second order effects on Australia would be material. In these circumstances, it may be that Australian portfolios would wish to make some select sales of stocks which have held up well to increase the cash buffer for future opportunities.

This Blog will inevitably be superseded by subsequent events. Let's hope for good news!

Happy Investing!



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