Trump's Tariffs: Is Free Trade a Thing of the Past?

The imposed tariffs by the Trump administration turned out significantly higher than initially expected

IN A NUTSHELL

— The US has announced tariffs on global US imports that are significantly higher than most experts had expected.
— Although we assume that the tariffs will not remain at this level in the long term, bilateral negotiations on tariff reductions are likely to be very difficult.
— A shift away from global confrontation towards global cooperation appears necessary to limit the damage to the economy and the stock markets.

Liberation Day

All imports to the U.S. affected by tariffs

U.S. President Donald Trump announced sweeping "reciprocal tariffs" on Tuesday night. All imports into the U.S. will be subject to a 10 percent tariff. However, much higher rates will apply to major trading partners: European Union, 20 percent; China, 54 percent; Japan, 24 percent; Taiwan, 32 percent; Cambodia, 49 percent; South Africa, 30 percent; Vietnam, 46 percent; Thailand, 36 percent, etc. The calculation of these tariffs is not easy to understand. Roughly speaking, the announced tariffs are 50 percent of the partner country's alleged tariff rate. This alleged tariff rate is calculated as the trade deficit with that country divided by imports from that country. The tariffs are scheduled to go into effect on April 9, but the previously announced 25 percent tariffs on autos and auto parts are effective immediately. Semiconductors, critical minerals, and pharmaceuticals are currently exempt but are likely to be subject to tariffs in the future.

Canada and Mexico are not mentioned in the new tariff announcements; what has already been decided will continue to apply. The White House said it would deal with these two countries based on a framework established in previous executive orders that imposed tariffs on Canada and Mexico as part of the U.S. government's efforts to combat fentanyl and border issues. Trump had previously set these tariffs at 25 percent before announcing some delays and exemptions. However, the debate over tariffs on Canada has also shown that Trump's actions have met with some resistance, even in the Republican camp. The push by Democratic senators to prevent tariffs on Canada was also supported by some Republican lawmakers, who then faced verbal attacks from the president.

It should be noted that the announced tariffs are higher than most observers and markets had expected. However, we expect bilateral negotiations to take place in the coming days and weeks to agree on some relief. However, the conditions for such negotiations are difficult, firstly because many talks have to take place at the same time, and secondly, and almost more importantly, the logic behind the tariffs has little or nothing to do with the actual tariffs. This means, for example, that a reduction in existing tariffs on U.S. goods cannot simply be used as a concession. These points could mean that the tariffs announced yesterday will remain in place for some time, with their full impact unfolding over the coming months and years.

Possible retaliatory measures

The European Union (EU) is expected to initiate negotiations as a first step, and only if these fail are tariff countermeasures likely. However, the EU has a trade surplus, which is likely to weaken its negotiating position. Retaliation against the U.S. could include non-tariff measures, such as the exclusion of U.S. companies from public procurement.

What if?

Yesterday's announcements are an unprecedented shock to free trade. For this reason, analysis based on historical data to classify them may be of limited accuracy. Nevertheless, to provide some insight, we estimate that all tariffs combined would increase the effective tariff rate on US imports from around 2.5 per cent to over 20 per cent if they remain in place. We estimate that this direct trade effect would lower U.S. gross domestic product (GDP) growth by about 60 basis points. Inflation could rise by as much as 1 percentage point. Major trading partners will also suffer from the announced measures. In nominal terms, GDP growth would be about 40 basis points lower in the euro area, 60 basis points lower in Japan and 130 basis points lower in China. Thanks to the agreement still in place between Canada and Mexico, they have been excluded from the wave. If tariffs were to rise by 10% in the future, GDP growth would shrink by about 150 basis points for Canada and 180 basis points for Mexico. Some of this has already been factored into our most recent forecasts. However, as mentioned earlier, these calculations should be treated with a fair degree of caution, as there will be a lot of negotiation and the current approach is unprecedented.

Uncertainty about future U.S. trade policy and possible countermeasures remains high, as there is still a risk of further escalation in the trade war. Even assuming that the U.S. will pursue a 10% tariff across the board, further rounds of tariffs cannot be ruled out. However, it should also be emphasized that we cannot underestimate the ability of global companies adapting to changing conditions. However, the back-and-forth of the past few weeks has had a very negative impact on confidence in the statements of the U.S. administration. Even de-escalating language from the U.S. would not really help to alleviate market participants' uncertainty about the future. We are in an environment in which it is becoming increasingly difficult for companies to invest, as there is currently no logical way to prepare for what may yet come. And the situation worsens with every day that passes without clarity. But the clock is ticking not only against (free) world trade, but also against Trump and his administration. If agreements are not reached quickly in bilateral negotiations, it could become difficult to repair the damage Trump is causing. At some point, it will no longer be up to the U.S. alone to turn back the clock.

The question therefore arises as to whether and at what point Donald Trump will be persuaded to back down and avert further damage to the U.S. and world trade. Or whether the U.S. president will be reined in by U.S. courts after all. The situation has, at the very least, deteriorated much more severely than had already been feared. Yesterday was just another step on the road from a globalized world to a much more protectionist one.

In summary, we do not expect the tariffs announced yesterday to remain at these levels for long. However, given the large number of parties involved and the lack of logic behind the tariffs, negotiations on possible relief will be very difficult and therefore protracted. On the other hand, the sheer implementation of the plans may reach its limits due to a lack of capacity in the U.S. administration or simply due to logistical problems. Finally, it remains to be seen whether the emerging political headwinds for Trump will also be reflected in a significant decline in his approval ratings, which could potentially lead to a change in the president's thinking. However, these are all hopeful signs that may take time to materialize. In the short term, the situation remains tense, and uncertainty is likely to remain the dominant feeling.

Asset-class implications

The initial market reaction to the tariff announcements was clear. With stock prices falling sharply around the world and government bond yields also falling, a scenario was clearly being played out in which fears of a sharp economic slowdown outweighed fears of inflation. And the latter in particular is likely to be a consequence of what Trump presented on Wednesday night. The dollar lost ground across the board, a sign that in this case the U.S. is part of the problem, not part of a potential solution. Shortly after the announcement, gold climbed to record levels, but then fell back relatively sharply. Since last night, Brent crude oil prices have lost about $4 per barrel.

Fixed Income & Currencies:

USD Rates:

US Treasuries saw a bull-steepening immediately after Donald Trump's tariff announcement, with yields falling significantly. The move continued in today's early New York trading. Trading volume climbed to 247 percent of the recent average, as the markets continue to appear risk-averse. With the intentions of yesterday's announcement still unclear, whether it is a basis for negotiations or a permanent change in tariff policy, Treasuries are likely to remain volatile for the time being. The market appears to be largely long, so it would not be surprising to see a sell-off if tariffs are lowered slightly as a result of negotiations. However, volatility could be exacerbated by upcoming data releases, such as Friday's employment report, as the market seems increasingly concerned about the labor market.

EUR Rates:

Not surprisingly, core eurozone government bonds have reacted positively. If implemented as announced, the tariffs could have a negative impact on growth. If maintained, a negative impact on global trade seems inevitable to us. Countermeasures by the EU, China and other countries are likely to exacerbate this drag. This is positive for interest rates, even if the impact on inflation is less clear. In addition, a typical risk-off move out of "risk assets" supports safe-haven[1] flows. The effect on non-core government bonds, government-related bonds and covered bonds is less obvious. A moderate widening of spreads versus Bunds in a risk-off environment is plausible, but we do not expect a substantial widening of spreads. Expectations of further rate cuts by the European Central Bank (ECB) support the view of a steep yield curve.

EUR IG Credit:

Trump’s tariffs led to a global risk-off move with its negative knock-on effect for EUR Investment Grade (IG) Credit. Cash bonds in EUR IG Credit have outperformed synthetic credit indices in the risk of move and we would call the credit spread widening orderly and no signs of panic or capitulation as the overall credit spreads are trading close to historic lows. The strong technical bid for the asset class remains intact as net new money is constantly coming into the market. The sectoral impact on tariffs needs to be drilled down in company-by-company analysis rather than bashing the whole market for collateral damage. If the dust settles, I stick to the view that the direction for credit spreads is set for further compression rather than a bigger sell off.

Asia Fixed Income:

Direct impact to Asian corporate with USD bond outstanding is considered limited, primarily in the pharmaceutical, steel, metals & mining, automobiles and semi-conductors' sectors. However, indirect impact such as weaker investment sentiment and slower growth going forward will have a bigger impact. In addition, the tariffs imposed by the U.S. will likely put more pressure on inflation and bigger impact on growth in the U.S.

Impact on the market from the above will likely have a bigger impact on high-yield credit, given any spread widening in the IG space is offset by the lower U.S. Treasuries yield. However, we expect Southeast Asian central banks will move sooner rather than later to a more accommodative policy to try and help absorb some of the shocks on their economy. Overall, total all-in yield remains attractive.

Currencies:

Normally, the U.S. dollar should benefit from U.S. tariffs on trading partners as the terms of trade shift toward the dollar. After the November election, the market behaved that way. As political uncertainty increased sharply, however, the focus of the currency market shifted to a potential recession in the U.S. A recession is clearly negative for the dollar. So far, the market has embraced this view, and the dollar has fallen sharply against European currencies. Asian currencies, on the other hand, lost

[1] Financial safe havens are investments or assets that are expected to retain or increase in value during times of market turbulence

against the dollar as the planned tit-for-tat tariffs are much higher and these countries have no capital to negotiate with the U.S. The current sharp move against the G10 currencies is also a function of the dollar's past success: Over the past five years, there has been a huge flow of capital into the U.S. because of the stock market's performance. That flow is now reversing. As market liquidity is not good, we would not rule out disruptive moves in the coming weeks.

Equities:

Diversification more important than ever as uncertainty rises

The measures unveiled in the Rose Garden are likely to have long-term and potentially painful consequences for global growth. As a result of the unilaterally announced global trade war, frightened consumers and policymakers will do only one thing: wait and do nothing. The cost of uncertainty is expected to be enormous and could grow by the day. Uncertainty about job security could increase; uncertainty about where and when to invest, whether and when to consume or travel. Diversifying portfolios across asset classes, sectors and geographies might be one potential way for investors to manage risk.

Risk case – recession

If none of the announced tariffs are reversed by deal-making in the next four weeks or so, the global economy risks entering an "oil price shock" type crisis by mid-year. Our previous earnings estimates and index targets would have to be revised significantly downwards.

In our view, only the most defensive equity sectors (telecommunications, utilities, consumer staples, healthcare) might perform relatively robustly in such a negative scenario. In our view, the sectors that have generated the highest returns for investors in recent years might be at the greatest risk of being sold off. Valuations are likely to fall, although we expect earnings cuts to be less pronounced. Cyclical sectors such as consumer discretionary, capital goods and enterprise software companies are likely to see the largest negative earnings revisions. While the U.S. has opened up the potential for a trade conflict with the rest of the world, every single country has its eyes focused on just one country - the U.S. This could mitigate some of the economic damage in the rest of the world. Markets outside the U.S. may continue to fall somewhat less than U.S. equity markets. European small- and mid-caps are more economically sensitive and are unlikely to outperform in such a scenario. In Asia, equity markets have been heavily impacted by the announced tariff, which exceeded market expectations. Japan and export-oriented Vietnam may continue experiencing selloff due to the unexpected tariffs. Domestic-oriented markets such as China, India, and Indonesia may show relative resilience compared to other regional markets. So far, Australia and Singapore have been less directly impacted by the tariffs with the lowest tariffs rate APAC. Domestic focused and defensive sectors in both Australia and Singapore are likely holding up better than other sectors.

Base case – deal-making

At this point, we are still hopeful that the coming days and weeks will provide enough time to avoid a full-blown trade war. More cars could be made in the US. US farmers could be allowed to export more products abroad. In his Rose Garden speech, Trump again referred to the stock market, keeping alive our expectation that he could intervene with supportive measures. As such, leaving portfolios unchanged as they are today might be the best decision. However, even in such a “deal-making”-case we expect that the upcoming Q1 reporting season will force consensus earnings estimates lower. The global economy and equity markets have shown amazing resilience while the world experienced a series of “black swan events” during the past 15 years (Euro Crisis, Chinese housing bubble, Covid, Ukraine war). A reversal from global confrontation to global cooperation will be needed to limit the damage to the economy and equities.

Liquid Real Asset:

As the global economy navigates the challenges posed by tariffs, growth is expected to slow, particularly in cyclical sectors such as retail. The macroeconomic landscape suggests the potential for further interest rate cuts, which could provide a boost to interest rate sensitive sectors. In listed real assets, this environment offers opportunities for growth, particularly in domestic infrastructure projects and defensive sectors such as senior housing.

Listed Real Estate:

While listed real estate will not be immune to the impact of the newly announced tariffs, the relative impact should be more muted given the bond-like characteristics with average lease durations of 5+ years. The net lease sector is a good example, with weighted average lease durations of over 10 years, and where the majority of tenants are investment grade, insulating landlords from a weakening economic backdrop. Other defensive sectors within publicly traded real estate that are less economically sensitive are seniors housing, as mentioned above, as the leases are all needs-based private pay, and the manufactured housing sector, which is growing in demand and is mostly age-restricted retirement communities. Finally, despite the negative headlines following the DeepSeek news, the data center sector has historically outperformed significantly during periods of economic uncertainty due to needs-based demand, 7-10 year leases, and consistent high single-digit earnings growth.

Listed Infrastructure

Within the listed infrastructure universe, we see little impact on the sectors. Most companies are domestic based companies, that sell essential services to domestic based customers giving the asset class a much more predictable and resilient cash flow stream. We see utilities and communications to have virtually no impact from higher tariffs, and if you look at the more procyclical sectors, we also expect little direct impact. A slowing economy and changing trade flows could impact the transport and energy names the most, and we will be monitoring the sectors for dislocations in price to spot potential entry points. To the extent that global growth slows more broadly, we think that infrastructure's defensive characteristics will be highlighted, and the cost of capital could even be affected positively if we see a major move down in interest rates. The domestic economy focus, with investments in infrastructure and defensive sectors, provides stability amidst global economic uncertainty. Overall, despite the global challenges from the tariff uncertainties, we expect the outlook for listed real assets remains positive, with attractive valuations offering opportunities for investors seeking stable returns in a volatile market.

Commodities

U.S. tariffs have a potentially broad impact across the commodities space. For most commodities, the prospect of a trade war could lead to concerns about demand, which would be a major headwind for the industrial metals and energy complex. Not surprisingly, commodities such as copper and aluminum, which have benefited the most from certain tariffs, now stand to lose the most. Energy commodities also face a potential backlash from slowing global trade. Specifically, potentially lower demand could exacerbate the imbalance in the already well-supplied crude oil market. Agricultural commodities are also of concern. With China being a prominent target of the tariff plan, and the tariffs being broad-based across other potential buyers, US grain export demand may also see a decline. Gold could actually benefit from the tariff plan. The risk of a potential global economic slowdown and rising inflationary pressures on consumer prices are both positive for gold. In addition, the short-term reaction of a weakening USD is also supportive for gold. Finally, after the initial shock of the tariff plans and possible retaliation from various US trading partners, we may see commodities come back into focus. Should inflation become more persistent, we may see broad-based commodities regain the attention of investors seeking to hedge against inflationary economic conditions.

Glossary

Bunds is a commonly used term for bonds issued by the German federal government with a maturity of 10 years.

Duration is a measure expressed in years that adds and weights the time periods in which a bond returns cash to its holder. It is used to calculate a bond's sensitivity towards interest-rate changes.

The European Central Bank (ECB) is the central bank for the Eurozone.

The European Union (EU) is a political and economic union of 27 member states located primarily in Europe.

The gross domestic product (GDP) is the monetary value of all the finished goods and services produced within a country's borders in a specific time period.

High-yield bonds are issued by below-investment-grade-rated issuers and usually offer a relatively high yield.

Investment grade (IG) refers to a credit rating from a rating agency that indicates that a bond has a relatively low risk of default.

The price-to-earnings (P/E) ratio compares a company's current share price to its earnings per share.

The spread is the difference between the quoted rates of return on two different investments, usually of different credit quality.

A tariff is a tax imposed by one country on the goods and services imported from another country.

Treasuries are fixed-interest U.S. government debt securities with different maturities: Treasury bills (1 year maximum), Treasury notes (2 to 10 years), Treasury bonds (20 to 30 years) and Treasury Inflation Protected Securities (TIPS) (5, 10 and 30 years).

A yield curve shows the annualized yields of fixed-income securities across different contract periods as a curve. When it is inverted, bonds with longer maturities have lower yields than those with shorter maturities.

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as of 4/3/25; 103369_5 (04/2025)

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as of 4/3/25; 105373_1 (04/2025)