CIO OFFICE MORNING MARKET WRAP

7 April 2025

Simply said, the tariffs announcement on ‘liberation day’ by the White House was the single most negative market event since the pandemic. Last week, expressed in US dollars, global stocks tumbled -8.5% in developed markets and -2.9% in emerging regions, while listed real estate fell -5%. US Treasury yields fell -20 basis points across the curve. The 12-month settled at 3.83%, the 2-year at 3.65% and the 10-year at 3.99%. Safe bonds benefitted, with global govies up +2.2%and quality corporate +0.9%, while riskier segments were affected by spreads widening: emerging debt lost -0.4% and global high yield -1.5%. Gold saw profit taking, down -1.5% to $3,038. Oil had a terrible week, between macro uncertainty from tariffs and the unexpected OPEC+ decision to massively increase supply. Brent lost $8 to $65.6. Finally, the dollar was down -1% against trade weighted counterparts, now close to -6% in 2025.

The White House announced a 10% baseline minimum tariff on all imports, starting last Saturday. The rate will increase on April 9th for countries with large trade deficits to specific rates communicated last week. The major ones are 20% for the European Union, 34% for China (on top of the “base” 20%, total 54%), as well as 24% for Japan and 25% for South Korea. This doesn’t include some sectoral tariffs already announced or to come. The formula for countries raised eyebrows as it was based on trade deficits, rather than actual tariff rates. The underlying concept seems to be that any trade deficit is unfair to the US, one way or another, which doesn’t make a lot of sense. There were other bizarre points in the giant list shown by President Trump: Taiwan (32% tariff) is not officially considered a country by the US, and one could wonder why the Falkland Islands, with their population of 4,000 people, are such a threat to America to deserve a 42% rate. This strangeness, combined with the very theatrical “Liberation Day” live show from the Rose Garden keeps alive the possibility of the spectacular first stage of a negotiation, in the purest “Art of the Deal” style: start a negotiation with an outrageous ask. We all remember the tariff saga on Mexico and Canada, which started with life-threatening levels but ended with a comparatively favorable regime for both, despite their (natural) trade surpluses with the US. It seems that the 10% baseline, in force since this weekend, may not be negotiable, but the additional layer is most certainly. Hopefully.

Nevertheless, it’s a massive shock. If we assume that it is implemented and stays at the announced levels with proportionated retaliation, the consequences are sinister for both growth and inflation, in America and elsewhere. China didn’t wait to announce a tit-for-tat retaliation on Friday, increasing the tariff rate on all US imports by 34% - which is actually a proper “reciprocal” calculation. The threat of a full-blown trade war is real even if last night both Japan and Indica signaled no retaliatory action, while Vietnam offered to remove all tariffs on US imports. As we highlighted in our 2025 Outlook, China is probably the only superpower that can afford to directly confront the US. But retaliation is also politically popular. The coming days will be crucial – and markets this morning are not showing any hope (more below).

Now let’s look at a medium-term horizon. Trump is in office for two months and is aggressively implementing his America First program, line by line, especially on government expenses and tariffs. He was elected on this platform, and we must keep in mind that this administration perfectly knows financial markets. Scott Bessent is a former hedge fund manager. Thinking that they didn’t take into account the risk of a stock rout is probably naïve. Other market developments clearly serve their objectives: the 10-year yield, the dollar, and crude oil in free fall. In a long interview two days ago, Scott Bessent said that the top 10% of Americans own 88% of equities. That is quite clear. The administration favors Main Street over Wall Street, and the scenario we highlighted in our Global Investment Outlook of “short-term pain for long-term gain” is probably their thinking. They know there will be pain, so they are frontloading it, in a race against time, hoping that the gains will come through before the November 2026 mid-term elections.

For our portfolios, we were obviously not expecting such a level of pain for risk assets (even if we are marginally underweight equities). Looking forward, this raises two questions. First, is it the end of the initial pain, and second, will the long-term gains actually happen?

For the first one, markets are always unpredictable on short-term horizons, and the volatility shock is big enough to trigger more selling from price-insensitive sellers (leveraged, gamma negative…). We however note that there is no sign of a US recession for now, with a strong US job report counterbalancing a relatively weak ISM services. US stock valuations are more reasonable (around ~18 times P/E, and just 3 more points for the Mag7), just before the Q1 earnings season, in absolute and relative to bond yields. Finally, with the VIX (US stocks volatility index) at 45, markets don’t need much good news to have some technical rebound. Of course, this will not happen if we enter a spiral of protectionism and trade war or if fear turns into panic. And we should not expect much help from the Fed, as chair Powell indicated it won’t rush to react to tariffs. For the second question, long-term gains are not compromised, if we assume that the US job market stays solid, that a significant part of the tariffs are negotiated lower, and that the combination of lower energy and financing cost helps the US consumer facing the inflationary shock from import levies. Of course, US corporate margins will take a hit, especially the most exposed to China imports (from Apple and Nike to retailers), and as part of the plan is also to tax more of the global added value of US mega companies in America, rather than, say, in Ireland. Yet at the country level, the future may see a much better situation, assuming we do not see a severe recession in the meantime. It’s a race against time, similar to what the Reagan administration did in the 1980s – it worked then, the US went through a severe recession, but it was understood and as the situation improved, he was triumphally reelected. That’s probably President Trump’s playbook. But the key difference is that Reagan’s mandate started in a crisis context, making hard medications easier to swallow for voters. We shall see.

We are not in short-term trading. As of Friday, the year-to-date returns of our well diversified recommended portfolios are +1% for the cautious, -1.7% for the moderate and -3.6% for the aggressive – after +5%, +10% and +13% last year and double digit returns in 2023. We will assess the current situation in detail in our upcoming investment committee this week. At this point, our overweight in government bonds with long duration and our full allocation to gold are perfectly playing their role.

Markets this morning:
It's another bloodbath as we write this morning in Asia. Stocks are down almost -10% in Hong-Kong, -6% in onshore China and Japan, -5% in Korea. Future contracts on Western indices are not better: -3% for both the US and Europe. US Treasury yields are materially lower: -14bps for the 2-year at 3.5%, and -8bps for the 10-year at 3.91%. The dollar is marginally stronger, gold is steady at $3,025 and Brent falls by $1.6 to $64 as Saudi Arabia slashed its flagship crude oil. CDS in Asia are surging in sympathy with other risk assets.

Upcoming key events/data:
The week ahead will provide CPI inflation reports for the US (and China) on Thursday, the University of Michigan Sentiment survey on Friday, and a few more. Beyond top-down data, the most important will be international reactions to the US tariffs – including the outcome of a EU "crisis" meeting today, and some official guidelines expected from the UK. Any intention to seriously negotiate the tariffs will be a positive, and any aggressive retaliation will hurt more. Finally, the Q1 earnings season starts, with US banks on Friday but also Samsung tomorrow. Beyond numbers, guidance and reaction to tariffs will be key, especially how they will adapt (an example being Mercedes Benz considering shifting some production to the US). Keep the long-term in mind, and have a great week.

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