

Liberation Day — *the art of the deal?*

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What has happened?

As widely expected, on 2 April President Trump announced reciprocal tariffs under the International Emergency Economic Powers Act (IEEPA), as he declared a national emergency over the size of the US trade deficit. While there is some hope that Trump may use this executive order as a starting point for negotiations, he has said that he could increase further the level of tariffs should any trading partners retaliate.

Tariff details

Starting on 5 April, the initial tariff level for all countries will be 10%, with significantly higher tariffs for many of the major trading partners. From 9 April, tariffs will go up further for countries with which US has higher trade deficits. While tariffs for the UK and EU were 10% and 20% respectively as expected, many Asian countries face significantly higher rates, for example Vietnam with 46% tariffs. China will suffer a further 34% tariff after a 20% increase was put in place earlier this year. Trade with Canada and Mexico is excluded for now, as part of their trade with the US is already subject to a 25% tariff announced earlier this year.

Economic effects of tariffs

There are two primary economic effects of tariffs:

1

Higher prices and inflation:

Higher tariffs increase the price of goods imported and sold in the US. These goods could either be used in the manufacturing of goods produced in the US (for example auto components) or sold as finished goods. This will lead to an increase in prices and therefore inflation, which will hit consumer real disposable incomes in the next few quarters. Economists estimate that US inflation may increase by 1% or more.

2

Impact on growth:

The second impact is on growth, and the US GDP growth rate is estimated to potentially fall by more than 1%. Economists estimate that the average tariff rate on US imports will increase to around 25%, which is worse than expected, and a level not seen since the 1930s. News of retaliation by the US' trading partners is already emerging.

How have markets reacted?



Equity markets

The tariffs were announced after US markets closed last night and markets are in a strong risk-off mode with US equities suffering the biggest falls in pre-market trading. The reactions in Europe have been a little more muted, with the UK market off just over 1% and the European equity market suffering falls of approximately 2%. In Asia, Japanese equities are down nearly 4%, while Asian markets such as China are holding up better.



Currency and bond markets

In currency markets, the US dollar has weakened markedly, trading at over 1.31 per pound sterling. Despite the fears for higher inflation, bond yields have fallen, reflecting their 'safe haven' status, as well as fears for GDP growth and how this might affect Central Banks' interest rate policies. Overnight, expectations for US rate cuts this year have risen to more than 3 cuts of 25bps.

What does Brooks Macdonald think?



At times like this when emotive media headlines are everywhere, investors should remain calm and focus on fundamentals. This is likely to continue to be a rapidly evolving economic narrative over coming months. While the global economic outlook is becoming murkier, there are assets which offer attractive valuations. For example, UK equities are relatively and historically cheap and low valuations offer a margin of safety, as well in many cases benefiting from sizeable dividend yields. More than ever, it is important to have a balanced, diversified portfolio, positioned for more than one economic outcome.

Important information

Investors should be aware that the price of investments and the income from them can go down as well as up and that neither is guaranteed. Past performance is not a reliable indicator of future results. Investors may not get back the amount invested. Changes in rates of exchange may have an adverse effect on the value, price or income of an investment.

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