

# Market View April

created by Ullrich Fischer, Chief Investment Officer

## Executive Summary

- The sharpest U.S. tariffs in 60 years have been announced, leading to the strongest single-day risk-off reaction in the markets since the pandemic. We expect negotiations will ultimately result in lower tariff levels and broader exemptions. Nevertheless, the risks to the global economy have undoubtedly increased.
- Political uncertainty is now reaching its peak. Both the flawed methodology behind tariff calculations and the absence of a transparent reaction function only add to market unpredictability. If the situation continues to escalate – which we do not currently expect – and the tariffs remain at this level for several months, a recession would be likely.
- Our base case remains a 14% equity correction, considered average from a historical perspective. Continued market deterioration could push the Trump administration to reconsider its aggressive tariff policies. Yet despite the current turbulence, we do not expect the bull market to end this year. Year three of a bull cycle often proves challenging.
- Weak US growth does not necessarily precede economic collapse. The current softness seems more related to a sequencing issue, where growth-negative (versus growth-positive) policies are advanced first, rather than a structural breakdown.
- Liquidity tailwinds are emerging, with the US Federal Reserve's indicated dovish shift and a weaker US dollar easing global financial conditions. This could create a favorable set-up for risk assets from mid-Q2 onward, though tariff uncertainty must first be resolved.
- As for the longer term, we expect a shift from a K-shaped, government-driven US economy to a more private sector-focused model, which will likely keep volatility elevated. Markets have been underestimating Trump's willingness to make drastic changes to drive this transition.
- Overall, we see promising opportunities on the horizon, particularly in Q2, but the current environment demands caution and a vigilant eye on the impact of geopolitical and monetary policies.

## Trump raises the stakes on “Liberation Day”

- Based on calculations from Goldman Sachs, the announced US “reciprocal” tariff policy implies a globally weighted average US tariff rate of ~18.8%, up from 2.5%. Starting 5 April, a 10% baseline tariff is set to target imports from all countries excluding Canada and Mexico. From 9 April, most major trading partners will face additional individual tariff rates based on their trade deficit with the US. One-third of total imports are exempt, including pharmaceuticals and semiconductors.
- Following the US administration’s “Liberation Day” tariff announcements, the US dollar has erased all gains made since Trump’s win in early November. The fall has been largely driven by concerns about potential capital repatriation and declining yield differentials.
- Apparel makers are leading the decline while bank stocks are also tumbling, a sign of worry about the broader economy. Cyclical stocks are underperforming defensive stocks.
- US equities and bond yields have now largely reverted to or below pre-election levels, as expectations for extraordinary US economic outperformance fade.
- Notably, gold is the year’s top-performing asset and a reflection of persistent uncertainty around global policy and central bank demand.
- In Q1 2025, the gap between US and European equity returns was one of the largest ever recorded. While steep relative selloffs often precede a bounce back, US equities remain more expensive than their global counterparts and could explain the persistent sense of caution.

## Market Development

### WORLD

- As JPMorgan notes, the US tariffs mark the largest US tax hike in nearly 60 years and could increase US inflation by 1.5 percentage points this year. On paper, the tariffs could generate nearly USD 400 billion in revenue, around 1.3% of GDP. If the tariffs are fully enacted and permanent, however, the blow to real incomes and spending could push the economy toward recession – even before taking retaliation or reduced exports and investment into account.
- A negative Q1 in US GDP growth is a real possibility according to the negative Atlanta Fed GDPNow estimate, even when adjusted for tariff front-running import effects. But hard data, despite tariff angst and other distractions such as DOGE, only point towards a slowdown rather than a recession, so far.

- Meanwhile, political tension in Washington is on the rise. Senate Republicans favor using a “current policy” budget baseline to justify further tax cuts without immediate spending cut offsets, clashing with House demands for USD 2 trillion in spending cuts to match the USD 4.5 trillion in proposed tax cuts. Internal GOP divisions and a tight deadline, with Memorial Day (end-May) as the goal, could get in the way. Any upside from fiscal stimulus would thus depend on first overcoming these hurdles.

## EUROPE

- The reaction of European automakers to the tariff announcements was relatively moderate, suggesting the impact may be largely priced in – but the apparel and clothing sectors were hit hard. The euro’s strength could stem from broadly expected proactive EU measures against US tariffs (including a potential emergency fiscal-support package) and further declining rate differential between the US and Europe. In terms of currency trading, the EUR/USD exchange rate is nearing the upper end of its medium-term range (1.02-1.12). A breakout would signal further EUR strength.
- EU tariff countermeasures could include a potential digital tax on the major US tech companies.
- British stocks could relatively benefit, as the UK is only subject to half of the EU tariffs. Due to the lower share of exports to the U.S., the United Kingdom could theoretically function as a trading hub for EU goods in the future.

## SWITZERLAND

- Switzerland faces a 31% tariff under the new trade rules. The US administration considers it a protectionist country, largely due to subsidies and import restrictions.
- According to initial analyst reactions, Swiss luxury goods and mid-sized industrials will be most affected while larger firms with US-based production may benefit. Pure domestic players should remain relatively safe. Pharmaceutical products are exempt, sparing around 6,000 items and limiting the impact on big pharma.
- The Swiss National Bank’s rate cut in March has made the Swiss franc the lowest-yielding currency globally.

## Scaling the peak of uncertainty

Although markets are forward-looking mechanisms, but they cannot effectively price in future benefits from pro-growth policies, namely tax cuts or deregulation, if the current environment remains this uncertain. Establishing a market bottom requires working through this volatility as uncertainty peaks.

The lack of reciprocity in Trump's so-called "reciprocal" tariffs is evident. Rather than being based on tariff or non-tariff barriers, the measures are calculated on the trade deficits by country – which makes it difficult for countries to formulate a coherent response. In essence, the approach exemplifies flawed policy design and execution.

The reciprocal-tariff formula itself is problematic: tariff rates are based on dividing a country's (goods-) trade surplus with the US by exports to the US and then halving the result. This approach disproportionately targets countries with significant trade surpluses while imposing a flat 10% rate on those with balanced trade or US surpluses. For instance, China's USD 295 billion trade surplus divided by USD 438 billion in exports results in a 34% tariff, while Japan's USD 74.14 billion trade deficit divided by USD 154.5 billion in imports yields a 24% tariff. Taken at face value, this system forces the affected economies to either reduce exports to the US or drastically increase imports from the US. Taking the formula at face value implies simply lowering tariffs on their end may not affect the US rates imposed.

Symbolism and stark inconsistencies, rather than sound economic analysis, appear to underpin this policy. It also demonstrates a fundamental misunderstanding of David Ricardo's theory of comparative advantage, which states that countries benefit most when specializing in areas where they hold a relative advantage.

One example is imposing a 32% tax on coffee imports from Indonesia, where the US exports little to no coffee. Tariffs are even being levied on the uninhabited Heard and McDonald Islands, remote parts of Australian territory.

## So what's next?

While the widespread outrage and risk-off market reaction are understandable, we believe that the tariff announcements should be viewed as opening bids in a series of negotiations rather than definitive policies. This is also what US Treasury Secretary Bessent signaled in an interview right after the announcement. Trump's history of imposing hefty tariffs only to later delay or adjust them, as seen with Mexico and Canada – both of which are notably exempt from the reciprocal tariffs – suggests a willingness to negotiate.

Our base case is that most of these tariffs will not be permanent, and the effective rate will significantly come down over time. However, the sheer aggressiveness of these figures elevates the risk of negative outcomes, including failed negotiations, for all involved.

The result of these negotiations will determine whether the policies lead to a manageable growth slowdown bottoming in Q2 or escalate into a full-blown economic crisis. Bilateral negotiations will likely dominate the landscape – not because they are the ideal strategy, but because there is no coherent framework or reaction function guiding the international response. Perhaps the hope is for a global convergence toward the 10% baseline rate.

In any case, the tariffs further increase the risks for both the US and the global economy, with a more pronounced negative impact on growth rather than inflation, we think. How the US Federal Reserve (Fed) interprets these developments will be crucial.

Recent comments by Fed Chair Jerome Powell suggest a possible dovish policy pivot, with attention shifting from fighting inflation to addressing growth risks. Two US jobs reports are expected before May's Federal Open Market Committee (FOMC) meeting, during which we expect a dovish pivot is possible if the economy continues to weaken.

## Positioning

In our view, April is likely to mark the peak of tariff-related uncertainty as negotiations begin. Markets are expected to endure continued, heightened volatility throughout this period. It's important to note that much of the current market weakness is politically induced and can be politically resolved – provided the situation doesn't spiral out of control. The pressing question now is: Where is the pain threshold for the Trump put and the Fed put?

For the time being, we anticipate underperformance in growth-sensitive equities, lower bond yields and a broadly weaker US dollar. As the evidence suggests, sizable tariffs would be detrimental to long-term economic growth expectations.

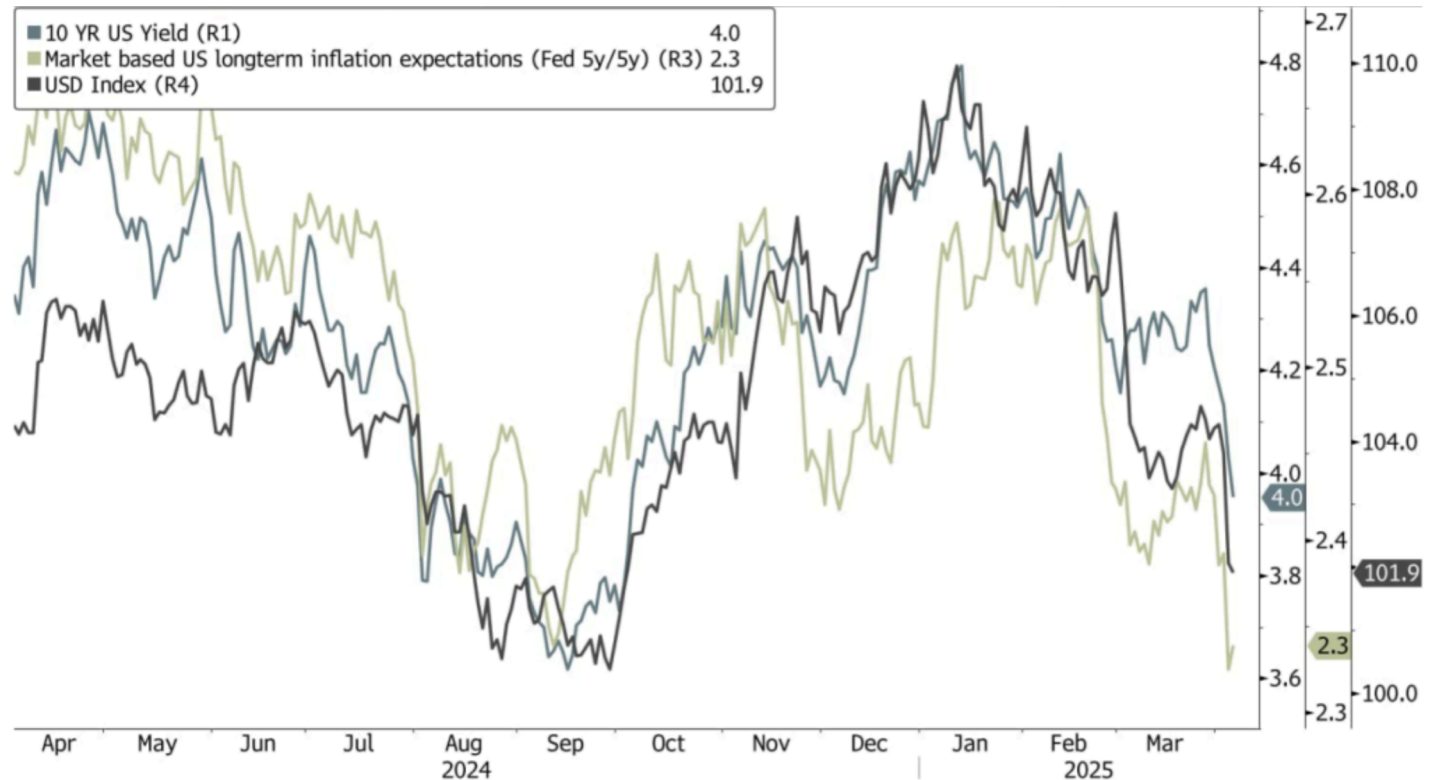
Historically, the S&P 500 has experienced an average drawdown of approximately 14% every 12 months. Our 2025 outlook had already predicted a similar pattern this year. Over the next few weeks, we expect these levels, especially as corporate share buybacks – typically a robust source of equity demand – are largely absent in the run-up to the next earnings season.

As we move into Q2, our outlook on US equities is more optimistic. Although US growth is slowing, the full-year trend remains above recessionary levels so far. A more dovish Fed and stabilizing earnings revisions could contribute to a more favorable set-up. A cleaner positioning in big tech stocks also enhances their appeal. However, we are approaching long positions cautiously (after taking several steps to reduce our equity allocation towards a neutral weighting in Q1). While there is not much interest in AI at the moment, reports indicate that the demand for Nvidia chips remains extraordinarily high.

We expect the Fed to adopt a more accommodative stance by May or June. In addition, we believe that the Trump administration will seek a tariff-exit strategy in Q2 and pivot towards pro-growth policies, focusing more on tax cuts. This combination could trigger a broader market rally in the second half of 2025.

Certain markets do seem to be emerging as relative winners under the announced tariffs, including the UK and Australia (both at the 10% baseline rate). Meanwhile, Europe and China appear to be performing well enough in the initial market response – likely in anticipation of domestic stimulus measures aimed at stabilizing growth. In China, recent pro-private sector policies, technological advances by DeepSeek AI and a consumption-led recovery are driving a more durable rally compared to last year's brief rebound. But if China devalues the Yuan in response to tariffs, this could trigger a major risk-off event globally. Gold remains structurally bullish over the long term but now requires cautious handling. Goldman Sachs has raised its year-end target to USD 3,300 per ounce, citing strong ETF inflows and ongoing Asian central bank demand that is projected to last for the next three years. While the fundamental case for gold remains strong, we believe the "Liberation Day" could represent a short-term top. A tactical rebalancing is advisable.

# Growth Fears Trump Inflation. Yields, Inflation expectations and USD in decline



Source: Bloomberg, per 04.04.2025

The market reaction is a clear indication that growth concerns outweigh inflation fears in the face of the tariffs. Market-based forward inflation expectations, long-term bond yields and the USD are all declining. While this trend could lead to a more dovish Fed and the easing of financial conditions, sentiment must first stabilize for risk assets to benefit. For that to happen, Trump needs to take a step back from tariff escalation in the coming weeks. A softer US dollar and declining bond yields typically benefit duration-sensitive assets like technology stocks and cryptocurrencies. If historical correlations hold, a new take-off stage could emerge in May.

Sources: Bloomberg, Morgan Stanley, Bank of America, Goldman Sachs, The Macro Compass, The Market Ear, Steno Research, 42Macro, JPM, Hightower Naples, FT, LBBW, BCA Research



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