



# Investment Views

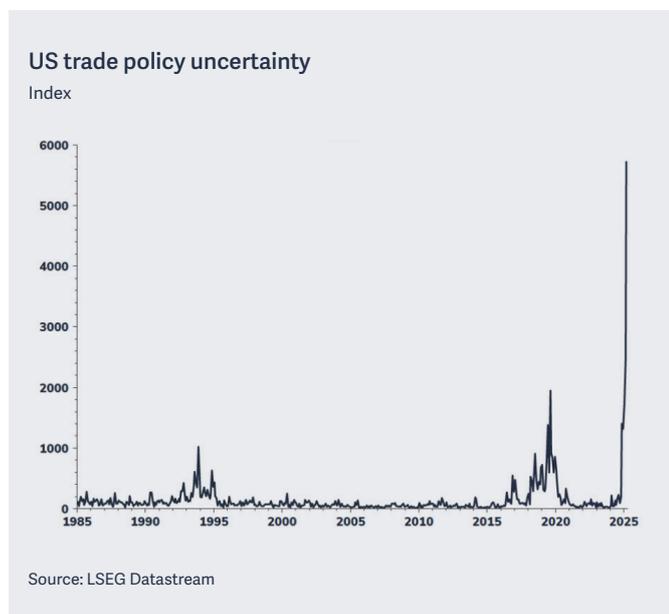
MAY 2025

## Past the point of peak uncertainty?

April 2nd was “US Liberation Day”, with President Trump announcing a series of sweeping tariffs to address what he described as unfair trade practices that disadvantaged American manufacturers and workers.

His “reciprocal tariff” strategy imposed a baseline 10% charge on imports from all countries (including more than 100 countries with which the US has a trade surplus), plus additional country-specific tariffs where his administration felt they merited it. Combined, the tariffs covered nations responsible for more than 75% of the \$3 trillion of goods the US imports each year. The move is part of Trump’s broader “America First” agenda, which seeks to protect U.S. industries and jobs but also raises concerns about the potential negative impacts on both the global economy and international relations.

As soon as the breadth and depth of the tariffs became clear, markets started to price in a large downgrade to growth expectations along with fears of higher inflation and a slower Federal Reserve policy response to lowering interest rates. Indeed, the implied growth downgrade on the first two days after the introduction of tariffs exceeded anything seen outside the initial COVID shock, one episode in the Global Financial Crisis, and Black Monday in 1987\*. As shown in the chart below, uncertainty regarding US trade policy also spiked to a level not seen for at least 40 years.



Even more concerning, US Treasury bonds, which are usually financial safe havens during crises, were not behaving as the textbooks say they should. Instead of yields falling, as investors sold riskier assets, yields rose with the rate paid on the 10-year UST rising 49 basis points in one week; the biggest increase for 20 years. When you borrow \$2 trillion per year, as the US does, that increase soon adds up. This was a clear message from the “bond vigilantes” that they had a dim view of the potential impact from tariffs. Thoughts of Britain’s experience in 2022 resurfaced, when Liz Truss attempted to address the cost of living crisis by announcing unfunded tax cuts, leading to a decline in the pound and an increase in mortgage rates. Maybe the US was not as safe as we thought it was.

As markets continued to gyrate, something had to give. So on 9th April came the announcement of a 90-day tariff pause being applied to most countries, along with some important product-specific exemptions to limit the impact on critical sectors. The obvious and notable exception was China, which saw no reduction in its tariff rate of 145%. China inevitably retaliated with its own tariffs of 125% on American goods. The percentages themselves are largely meaningless, given that little trade is likely to take place with rates anywhere close to those levels.

The global trade war thus morphed into a US-China standoff, with both sides digging their heels in, at least publicly. The US has signalled it wants other countries to limit trade with China as part of any deal that provides access to the US market. For its part, China has said it will “never kneel down” before Washington, restricting the export of critical minerals used in batteries and high-tech applications and sending its leaders on a charm offensive, touring the world to push back against US influence and support its own export markets. In the meantime, trade between the world’s two largest economies continues to grind to a halt, sparking a corporate backlash. Jamie Dimon, Chief Executive of JPMorgan Chase, publicly urged Washington to engage with Beijing before the US faces challenges to its credibility.

What happens next? On the one hand, hedge fund billionaire Bill Ackman believes China will need to strike a trade deal with the US quickly. In his view, a drawn-out trade war will severely damage its economy, as every company with a supply chain in China will consider relocating to India, Vietnam, Mexico, the US or elsewhere. Maybe, but that all takes time and in the interim, sectors heavily reliant on international trade such as technology and manufacturing, are experiencing supply chain disruptions. Ford, for example, said it expects a \$1.5bn hit to this year's profits, and it is far from unique in withdrawing its financial guidance due to the industry-wide disruption.

Other economic commentators, such as the FT's Martin Wolf, says China is "huge, able and determined...with powerful cards", not least that many countries already do more of their trade with China than with the US. China is also arguably now a more reliable partner, and it may be easier for China to replace lost demand than it is for the US to replace missing supply, especially for critical components. Perhaps, but since exports accounted for around a third of China's growth last year, China may grow at a rate closer to 3% than the much-needed 5% this year. Recent production figures from China's factories confirm that it is already feeling the pain, with the April new export orders figure the lowest since Covid-19 ravaged the country in 2022.

Whichever side may be right, one thing that should be clear to all parties is that a drawn out conflict will leave no one better off. Neither side wants to blink first, but the recently announced planned talks in Switzerland are a big step in the right direction. Yes, some damage has been done and the risk of recession is higher than it was, because globally tariffs will be higher at the end of the year than they were at the beginning. In the near term, uncertainty will remain elevated, but we appear to have passed peak fear with risk markets responding positively to the April 9th U-turn. Longer term, real signs of a visible improvement in US-Sino relations along with a permanent shift in the tariff policy would be a genuine catalyst for this recent rebound to prove sustainable. Ultimately, the world needs a US that competes and co-operates with China. After all, at \$700bn, China is the second largest owner of those US Treasuries we mentioned.

(\*source: Goldman Sachs, 8.4.25)

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