azimut

AZIMUT GLOBAL VIEW

03.02.25

Main Events

US NFP
After a blockbuster data in December, the US labor market is expected to return to a more moderate pace of job creation

07.02

US CPI
Any upside surprise on inflation may further delay the timing of the next Fed rate cut

12.02

US RETAIL SALES
Retail sales ex-auto are expected to continue to grow at a healthy pace

14.02

JAPAN GDP
The Japanese economy is expected to have grown at an annualized rate of 1% in the 4Q

17.02

Azimut Global Network

- Milan
- Abu Dhabi
- Austin
- Cairo
- Dubai
- Dublin
- Geneva
- Hong Kong
- Estoril
- Istanbul
- Lugano
- Luxembourg
- Mexico City
- Miami
- Monaco
- New York
- Santiago
- São Paulo
- Shanghai
- Singapore
- St Louis
- Sydney
- Taipei

TARIFF SCHIZOPHRENIA

- **After announcing 25 percent tariffs on Canada and Mexico set to take effect in February, Trump withdrew them shortly before their implementation in exchange for an increase in border patrols**
- **If implemented, tariffs are likely to lead to margin contraction and/or a resurgence of inflation, while uncertainties about their enforcement discourage business investment and trigger disorderly reactions in financial markets**
- **The U.S. threat to impose tariffs even on historically friendly countries could benefit China, prompting some nations to seek closer ties with the Asian giant**

The prediction in the annual outlook that 2025 would be a more volatile year, mainly because of Trump, was an easy one and unfortunately spot-on.

Just after he was sworn in, Trump threatened Canada and Mexico with 25% tariffs on imports from the two countries. Initially scheduled to take effect Feb. 1, they were delayed until Tuesday. Then, on Monday, after a phone call with the Mexican president, Trump decided to postpone the effectiveness by a month, in exchange for a commitment of more troops to patrol the border. As the drafting of this prologue neared completion, Canada received similar treatment in exchange for a similar commitment.

The implications of this strategy—using tariffs as leverage in foreign relations—are numerous and far-reaching.

The first and most simple consequence is that companies are discouraged from investing. To decide whether to build new plants, enter new markets, or relocate production, businesses need the ability to make multi-year forecasts. If the rules of the game can change overnight, investments that once appeared profitable may become unviable. In an environment of heightened uncertainty, companies may reasonably hesitate to invest, ultimately reducing a country's long-term growth potential.

(continued)

The second consequence is that tariffs, if applied, increase final costs and reduce efficiency. This is indisputable and based on Ricardo's theory of comparative advantages. Businesses will either absorb the higher costs, leading to lower margins and reduced profits, or pass them on to consumers, fueling inflation. The consequences could be even worse should the other country respond with retaliatory measures. So far, Trump has been vocal in targeting countries where he believes he can inflict significant economic damage. However, other countries or regions, such as China or Europe, may be less conciliatory, as well as responding with retaliatory measures. Neither shrinking profit margins nor rising prices—leading to tighter monetary policies—is favorable for markets. Moreover, numerous studies indicate that tariffs typically result in lower economic growth.

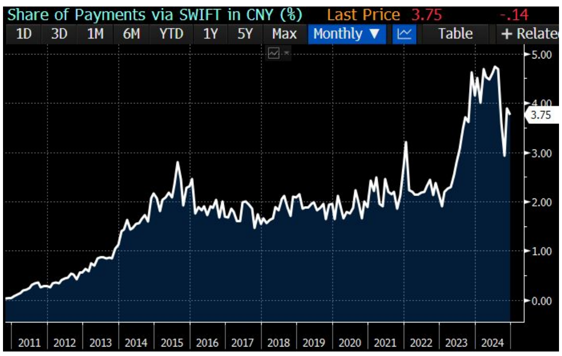
Consider the automotive industry as an example. After the nearshoring of recent years, many American companies have moved production to Mexico. Several recent estimates agree that if Trump were to actually impose 25 percent tariffs on Mexican imports, the average price of cars for American consumers would rise by approximately $3,000.

The third consequence is that this yes/no/maybe tariffs approach only fragilizes markets. Although the threat of tariffs on Mexico and Canada had been circulating for days, markets did not take it seriously assuming it was a negotiating tactic. The Mexican peso had even strengthened against the dollar compared to pre-Trump levels. However, when it appeared that the tariffs might actually be implemented, markets had disorderly reactions, with stock markets falling between 2 percent and 3 percent and the dollar rising sharply - only to reverse course and close the day unchanged once Trump's bluff became evident.

These abrupt movements do nothing but cause stop losses to market participants, especially in an environment of high leverage and risk appetite.

Beyond that, Trump's repeated pattern of threatening tariffs—only to retract them shortly after—has conditioned markets to discount tariff risks altogether. This has already happened three times (including Mexico, Canada, and previously Colombia). As a result, markets may assume future tariff threats are mere posturing rather than real policy risks. But, it cannot be ruled out that sooner or later tariffs will actually be implemented. Indeed, it would even become necessary at some point to prevent Trump from losing all credibility both with the countries he wants to deal with and with those who elected him precisely on his electoral pledges. Thus, the fourth possible consequence is that because of this schizophrenic use of tariff threats, we might see abrupt market movements should they actually be imposed, because the market would not have priced them ex-ante at all based on previous experience.

The final, but by no means least significant, consequence of this tariff strategy is that it serves as an unintended gift to China in an increasingly polarized world dominated by two superpowers. Trump's repeated tariff threats against long-standing U.S. allies are perplexing and risk prompting these traditionally Western-aligned countries to reconsider their international alliances—potentially strengthening ties with China. This is even more true for countries, typically developing countries, that have increasingly gravitated around China over time and do not necessarily have strong or good relations with the United States. Toward most of these emerging or frontier countries, China has proven to be a very reliable partner in the long run, delivering on its promises.



Source: Bloomberg

Source: Bloomberg

(continued)

As a reminder, the first blow to the credibility of Western institutions toward developing countries occurred following the invasion of Ukraine. At that time, Russian central bank reserves held abroad were confiscated, in violation of international conventions. It was a warning that holding Western assets, or having assets deposited in Western countries, could result in their expropriation following unilateral decisions by Western countries.

The consequences can be seen in the two graphs on the previous page. The share of international payments made in Chinese Renminbi has risen significantly post-2022, reflecting that in international trade with China, some countries are increasing the share of transactions settled directly in renminbi, without passing through the US dollar anymore. The other evidence is that between 2022 and 2023 China rapidly reduced its holdings of U.S. Treasuries while raising its gold holdings (in orange, inverted scale). After pausing for almost a year, these trends seems to have resumed just after Trump's election.

Everything considered, if the threat of imposing draconian tariffs was only used to get a cheap bargain of a few more border patrols, perhaps it was not worth it.

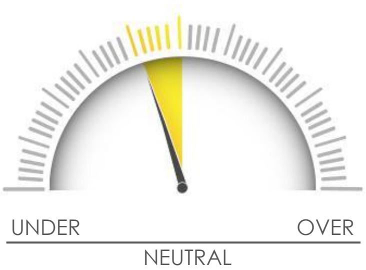
Asset Allocation View

Equity			
Developed Markets	**Downgrade**		
Emerging Markets	**Downgrade**		
Fixed Income			
Developed Markets Sovereign			
Developed Markets Corporate			
Emerging Markets			
Commodities			
Currencies		*Commentary below*	

UNDER NEUTRAL OVER

Equity

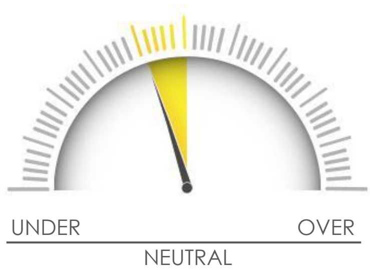
Developed Markets



We have lowered our recommendation on Developed Market Equities to **Slightly Underweight**. The uncertainty surrounding the potential implementation of broad-based tariffs introduces an additional risk factor that, by itself, warrants a higher risk premium. If these tariffs are enacted, they could have even more pronounced negative effects on inflation and economic growth. Furthermore, the recent release of artificial intelligence applications by DeepSeek and Alibaba—capable of competing with their U.S. counterparts—may contribute to a reduction in the valuation premium currently enjoyed by U.S. technology companies. Given these factors, along with markets still trading near their highs, we believe a more cautious stance is warranted.

US	Europe	Japan

Emerging Markets

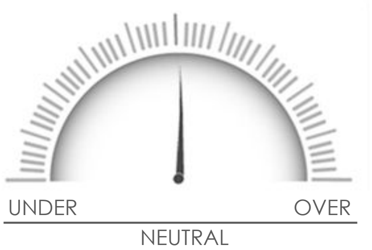


We have also reduced our recommendation on Emerging Markets Equities to **Slightly Underweight.** Emerging countries could be more vulnerable than developed countries, if the United States implemented large-scale tariffs. Partially offsetting this, valuations in these markets continue to trade at a significant discount compared to developed countries. This gap may help explain the resilience shown by emerging countries during recent episodes of volatility. In addition, the absence of direct tariff threats against China—contrary to initial expectations—could serve as an additional source of relative strength for the country.

Asia ex-Japan	EEMEA	LATAM

Fixed Income

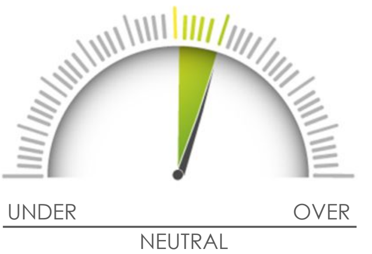
Developed Markets Sovereign



We have maintained our **Neutral** recommendation on Developed Markets Sovereign Bonds. The imposition of tariffs increases the risk of higher inflation in the United States, but also a slowdown in the global economy. The impact on U.S. bonds is therefore mixed, while bonds in the rest of the world could benefit (rates might go down). In addition, bonds could act as a portfolio hedge in case of a correction in equity markets, as has been the case in recent weeks. It is therefore recommended to maintain a neutral exposure.

EU Core	=	EU Periphery	=	US Treasury	=	Japanese JGB	=

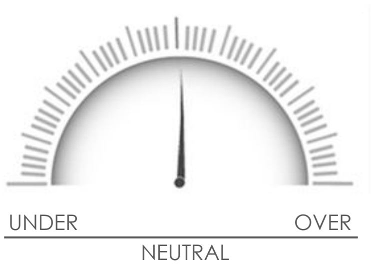
Developed Markets Corporate



We have kept our **Slightly Overweight** recommendation on Developed Markets Corporates. Trump's threats on tariffs should not have an impact on corporate bond spreads for the moment. Therefore, the search for yield in the fixed income market will continue to favor the asset class. Within corporates, we maintain a preference for investment-grade bonds over high-yield bonds that are hovering around all-time lows.

IG Europe	+	IG US	+	HY Europe	−	HY US	−

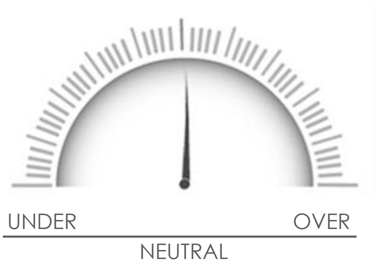
Emerging Markets



We have kept our **Neutral** recommendation for Emerging Market Bonds. The potential risks posed by tariff impositions from the Trump administration are mitigated by the relatively higher spreads that emerging market bonds currently offer compared to similarly rated corporate bonds in developed markets.

Local Currency	=	Hard Currency IG	=	Hard Currency HY	=

Commodities



We maintained our **Neutral** recommendation on Commodities. Among these, we remain more positive on precious metals, which could benefit both in the event of lower-than-expected tariffs resulting in a weaker dollar and/or fears of further fiscal slippage.

Precious	+	Energy	=	Industrial	=	Agricultural	=

Currencies

The Committee kept the **Neutral** stance on the US Dollar. Uncertainties related to the imposition of tariffs by the United States is likely to continue to create unusual volatility on the dollar exchange rate. Nonetheless, the dollar currently trades in line with the level suggested by the rate differential, and barring any unexpected decisions on tariffs may continue to remain around current levels.

The view on the Euro remains **Neutral** as well. The euro also trades in line with fundamentals, but the main uncertainty remains US tariffs. Trump recently said that the next target after Mexico and Canada might indeed be the European Union. Should they be implemented, a further weakening of the single currency is possible.

The view on the **Chinese Renminbi** remains **Neutral**. The resilience shown by the Chinese market in recent weeks, along with technological advances on artificial intelligence, could encourage a resurgence of interest in the country, offsetting the lack of concrete news on fiscal stimulus.

The outlook for other **emerging market currencies** remains **Neutral**, waiting for more clarity on the potential tariffs by the U.S. government.

Euro	=	USD	=	CNY	=	Other EM	=