EDMOND DE ROTHSCHILD

EDMOND DE ROTHSCHILD ASSET MANAGEMENT

MARKET FLASH: US CUSTOMS TARIFFS ARE A FLOATING THREAT TO GLOBAL TRADE

- **Washington sent letters to several countries announcing between 20-50% in tariffs and additional levies on products and goods that are re-exported to third countries as a way of sidestepping the increases.**
- **France set an ambitious target of 4.6% for the government deficit in 2026. Meanwhile, the UK is struggling with a weak economy but that will allow the Bank of England to cut rates.**
- **In China, consumer prices rose slightly but production prices continued to suffer from deflation.**

Donald Trump stepped up the pressure on trading partners in an attempt to accelerate deals. He said August 1st would be the deadline for agreements. Washington sent letters to several countries announcing between 20-50% in tariffs and additional levies on products like copper (50%) and goods that are re-exported to third countries as a way of sidestepping the increases. Drug imports could be taxed by as much as 200% from 2026. The US president's initiative appears to have a political edge too: countries aligned with BRICS policies might be subject to a 10% surcharge and Brazil, because of its treatment of former president Jair Bolsonaro, could see its tariffs rise from 10% to 50%. Donald Trump also warned the European Union. Even so, the talks go on as European countries look for concessions on key economic sectors. Any agreement would be a good sign for the economy and higher inflation risks would be avoided if Europe decided not to retaliate. In that case, the ECB could proceed with a final rate cut. However, there could be a lasting impact on US inflation if trade uncertainty were to last until 2026. Lack of visibility on the trade war and its consequences could leave the Fed in rate-cut gridlock.

France, meanwhile, set an ambitious target of 4.6% for the government deficit in 2026. The UK is struggling with a weak economy but that will allow the Bank of England to cut rates. In China, consumer prices rose slightly but production prices continued to suffer from deflation due to industrial overcapacity and soft demand because of trade tensions.

Oil stabilised around $67 despite OPEC+ increasing production.

But despite the uncertainty, markets are reassured and are hoping for a good trade deal with the US. We are slightly underweight equities, especially in the US where valuations are demanding even if results should be less disappointing than expected. In government bonds, we are looking for entry points, especially in euro countries where bonds are back to attractive levels and which now better reflect Germany's fiscal stimulus. For the moment, we are overweight corporate debt. We are keeping a close eye on 10-year inflation expectations and oil, as well as US equity volatility which is too low given current risks.

Generally speaking, we believe bond markets have discounted risk factors more than equity markets.

EUROPEAN EQUITIES

Autos and tech led gains as European equity markets ended the period higher on hopes for a trade deal with the US. The extent and rollout of any deal are still not clear but hopes revived in the last few days that a framework agreement both with Europe and China might be reached. Industries exposed to China also rose on hopes that Beijing might provide additional stimulus, especially in the property sector. Basic resources were also lifted by rising copper prices after Donald Trump confirmed that a 50% tariff would be slapped on imports from August 1st.

In company news, **Brunello Cucinelli** announced, as expected, a robust 10.2% rise in first-half revenues. Elsewhere, advertising giant **WPP** issued a profits warning for 2025. The group cited difficult macroeconomic conditions and lower-than-expected net new business. The announcement augurs badly for other companies in the sector which are expected to report results in the coming weeks The tech sector saw some consolidation: **Capgemini** lost 6% when it announced the acquisition of **WNS** for $3.3bn. Private equity group **Blackstone**, along with other investment funds (and probably **Bouygues** and **Orange**), is mulling a bid on the telecoms group **SFR**. In the industrial software space, rumours in the US that **Autodesk** might bid for **PTC** boosted speculation around **Siemens**, **Schneider** and **Hexagon** in Europe. And **Meta** bought a 3% stake in **Essilor Luxottica** as part of a connected eyewear partnership.

US EQUITIES

Wall Street trod water with the S&P 500 gaining 0.04%, the Nasdaq 0.15% and the Russell 2000 0.65%. The US political mood remained agitated. The Trump administration decided to extend the deadline for trade discussions to August 1st. The proposed tariff on copper imports was viewed as damaging for many US industries, ranging from auto makers to producers of household electrical goods.

The tech sector continued to gain ground. **Nvidia** rose 3% to become the first ever company worth more than $4 trillion. As part of its ongoing hiring drive for its new AI division, **Meta** (+1.1%) poached Ruoming Pang, a top Apple engineer. AI specialist **CoreWeave** acquired **Core Scientific** for $9bn to improve its data centre presence.

In consumer discretionary, **Tesla** fell 1.7% after Elon Musk launched his own political party. Deliveries at **Boeing** (+4,7%) returned to 2023 levels. The bounce was seen as a positive indication of new CEO Kelly Ortberg's strategy to restore the ailing group's fortunes. **Delta Air Lines** (+11.6%) raised third-quarter guidance, citing stable demand after several quarters of decline.

In consumer staples, **Conagra** (-7.1%) said it expects flat sales this year so no short-term improvement. Sector consolidation continued. After last week's acquisition of GMS by Home Depot, **TopBuild** (+10.7%) paid $810m for Progressive Roofing.

Healthcare outperformed but trading was volatile. Takeover bids continued apace: **Merck** (+3.8%) bought **Verona Pharma**, an oncology and lung disease specialist, for $10bn. Biotech **Moderna's** cost-cutting strategy since the pandemic is starting to bear fruit: the stock jumped 12.4% over the week.

This week's winning sectors were energy (+2%), industry (+0.9%) and materials (+0.5%). On the downside, financials and communication services both lost 0.9%.

EMERGING MARKETS

The MSCI EM index closed flat in USD this week as of Thursday. South Korea, China, and Taiwan advanced 2.54%, 0.59% and 0.25%, respectively. Brazil, India and Mexico shed 5.56%, 2.15% and 0.71%.

In **China**, June PPI fell 3.6% YoY or more than the 3.2% expected, while consumer prices surprised on the upside, rising 0.1% YoY vs expectations for a 0.1% drop, and putting an end to four months of decline. The US Secretary of State will meet China's Foreign Minister in Kuala Lumpur for trade negotiations. Seven departments jointly issued opinions on the construction of a childcare service system. The NDRC is considering expanding the funding channel to include ultra-long-term special Treasury bonds to buy back completed housing inventory. The government hosted meetings to implement moves towards 'Anti-Involution'.

In **Taiwan**, technology-related exports continued to see strong momentum with June exports rising 33.7% YoY vs. the 27.1% rise expected, while exports to the US were up 90.9% YoY. **TSMC**'s second-quarter 2025 sales, excluding currency impacts, beat guidance at the high end on robust AI demand.

In **Korea**, the central bank kept the benchmark rate stable at 2.5%. The government will start to distribute cash vouchers to all citizens. Trump postponed the application of his 25% reciprocal tariffs on Korea to August 1. **Samsung Electronics**' second-quarter 2025 prelim results missed the consensus, mainly due to the delayed earnings recovery in semi divisions.

In **India**, Prime Minister Narendra Modi and Brazil's President Lula da Silva signed six agreements to expand the horizon of the cooperation between the two countries in sectors such as energy, agriculture and technology. The Defence Ministry is seeking to increase the share of its expenditure in GDP from 1.9 % to 2.5 % over the next five years. India's domestic pharma market grew 11.5% YoY in June, an acceleration vs. May's 6.9% rise. **Titan** preliminary reporting indicated sales growth lower than consensus, but in line with guidance. **Kotak Mahindra** surprised on the upside as first-quarter 2026 credit rose 14% YoY, outperforming the system and expectations. **TCS** reported a weak quarter with headline numbers missing consensus expectations. **JSW Group** plans to raise its stake in **JSW MG Motor India**, its car manufacturing joint venture with **SAIC Motor**.

In **Brazil**, June inflation came in at 5.35% YoY, or in line with expectations. May retail sales rose 2.1% YoY, or less than the 2.6% expected. President Trump threatened Brazil with 50% tariffs because of the decision to put former president Jair Bolsonaro on trial.

In **Mexico**, June CPI rose 4.32% YoY as expected. Spanish foreign direct investment in Mexico surged 69% in 2024 to 3.3bn. Automotive production in June rose 4.9%. YoY and exports increased by 14% YoY. **CIBanco**, **Intercam** and **Vector** won a temporary reprieve from US money laundering sanctions.

CORPORATE DEBT

CREDIT

The July 4th US independence holiday marked the beginning of the summer break and bond market trading calmed down. 10-year US Treasuries and German government bonds traded in a narrow 6bp spread with moves on the Xover limited to 10bp. This stability is in marked contrast to Donald Trump's very busy agenda: he returned in force to the tariff subject but pushed back increases to August 1st.

Low volatility persisted on credit markets, partly because of a significant fall in new issuance. July is traditionally a good month for credit markets due to black-out periods. With new money inflows continuing, technical factors are still favourable. Bonds have recently outperformed derivative products. However, spreads on dollar-denominated investment grade bonds are now at a year low. Over the short term, interest rates, which are still high, should be the main drivers behind total returns.

GLOSSARY

• Investment Grade: bonds rated as high quality by rating agencies.

• High Yield: corporate bonds with a higher default risk than investment grade bonds but which pay out higher coupons.

• Senior debt benefits from specific guarantees. Its repayment takes priority over other debts, known as subordinated debt.

• Debt is considered to be subordinated when its redemption depends on the earlier payment of other creditors. To offset the higher risk, subordinated Senior debt has priority over other debt instruments.

• Tier 2 / Tier 3 : subordinated debt segment.

• Duration: the average life of a bond discounted for all interest and capital flows.

• The spread is the difference between the actuarial rate of return on a bond and the rate of return on a risk-free loan with the same maturity.

• The so-called "Value" stocks are considered to be undervalued.

• EBITDA: Earnings before Interest, Taxes, Depreciation, and Amortization.

• Quantitative easing describes unorthodox monetary policy from a central bank in exceptional economic conditions.

• Stress Test: a process which simulates extreme but possible economic and financial conditions so as to assess any impact on banks and measure their resilience to these events.

• The PMI, for "Purchasing Manager's Index", is an indicator of the economic state of a sector.

• AT1s belong to a family of bank capital securities known as contingent convertibles or "Cocos". Convertible because they can be converted from bonds to shares (or depreciated entirely) and contingent because this conversion only occurs if certain conditions are met, such as the issuing bank's capital strength falling below a predetermined trigger level.

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