Monthly Macro Insights — April 2025

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Global growth remained relatively resilient in early 2025. However, front-loading of global trade flows, particularly between Asia and North America, greatly distorted the reality. In fact, stagflation and recession risks have both increased significantly.

Trump's vision...

US President Trump announced on 2 April the biggest escalation in US tariffs in a century, with a 10 per cent baseline tariff on imported goods. Some countries will also face individual tariffs of up to 49 per cent[1]. Certain sectors such as pharmaceuticals and semiconductors have been exempt for now, but more tariffs are coming. The strategy has been described as an effort to build up leverage and resources to manage US debt, reset its industrial base, and renegotiate its standing in the global order.

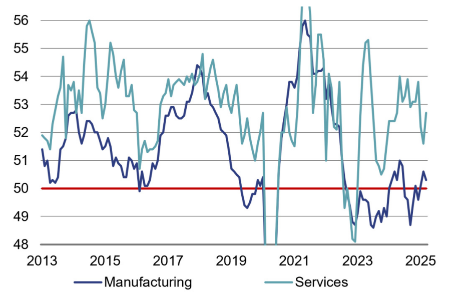
Regarding the latter, tariffs are being deployed alongside a deliberate reshaping of global alliances. These tariffs serve as leverage, offering relief to allies who align with US priorities, while imposing higher costs on those who do not.

Regarding public finances, the most recent projections from the Congressional Budget Office confirm once again that the US fiscal outlook is on an unsustainable path, increasingly driven by higher interest costs which in 2024 totalled USD 881 billion[2], surpassing other components of the federal budget. Since the Federal Reserve seems in no hurry to lower interest rates, the Trump administration believes that by introducing sweeping tariffs, it is creating precisely the kind of economic uncertainty that drives investors toward safer assets such as Treasuries, thus pushing yields lower. In addition, if imposed on a permanent basis, the 2025 new trade policy would increase tax revenue for the federal government by more than US$2.5 trillion between 2026-35[3]. Furthermore, spending cuts have been implemented while cutbacks, driven by Musk's Department of Government Efficiency, have seen thousands of federal workers lose their jobs. Overall, lower borrowing costs, higher revenues and tighter spending would lower the debt burden.

But arguably the most important pillar of the Trump strategy is growth, with tariffs serving as the ignition switch for a supposed manufacturing revival. Indeed, by making imports more expensive, Trump thinks he will create space for US producers to step back in.

World - Business confidence

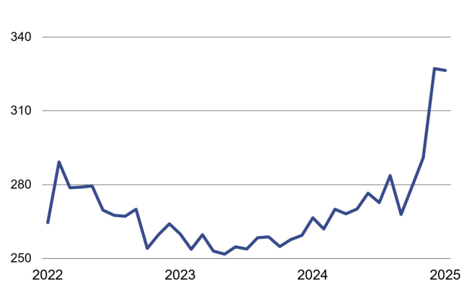
S&P Global Index



Source : Macrobond, Rothschild & Co Asset Management, april 2025

United States - Goods imports

in billion USD



Source : Bloomberg, Rothschild & Co Asset Management, april 2025

... is facing reality

Economists have long understood that higher tariffs do not, in general, reduce trade deficits. In fact, global data indicate that countries with higher tariffs actually have higher trade deficits.

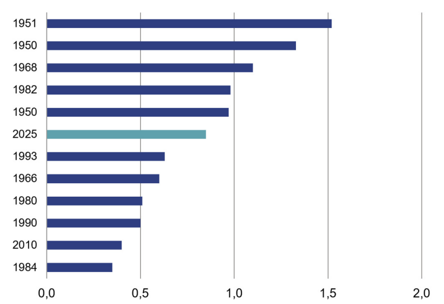
Although the new policy was supposed to be calibrated to offset trade partners' tariff, nontariff, and currency barriers to US exports, it was instead completely arbitrary and focused only on bilateral trade balances, which in many ways are a healthy reflection of comparative advantages. For example, the US imports aluminium from countries that can produce it most efficiently, such as Canada, while embodying it in exports, such as aircrafts, where it has the advantage. This will tend to lower US trade balances with efficient aluminium producers, and raise them with aircraft importers.

In fact, the very countries that have retooled their economies to serve US needs have been rendered disproportionately uncompetitive as the tariffs on them are higher. In turn, US importers will switch from high-to-low-tariffed countries. For instance, buyers of garments will shift their purchases from Bangladesh (37 per cent tariff rate) to India (26 per cent tariff rate). In the process, they will incur switching costs, but also uncertainty. As a result, the bilateral balance with Bangladesh will improve while those of India will worsen. Will the US administration then decide to raise the so-called "reciprocal" tariffs for India and lower them for Bangladesh? In the end, however, Indian-made garments may replace those from Bangladesh, but US-based factories will remain greatly uncompetitive with both of them.

Overall, to think that the bilateral balance is caused by trade barriers overlooks the fundamental reason why countries trade. The recent bout of unpredictability also risks robbing the US of one of its important and differentiating edges: long-term investor confidence in policy framework and decision-making.

United States - Tax hikes

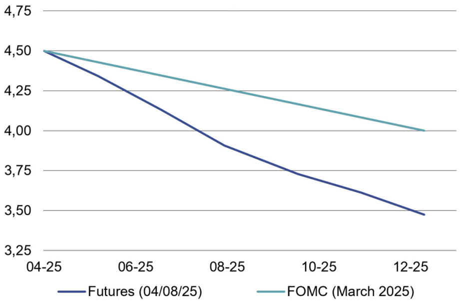
in % of GDP, since 1950



Source : Tax Foundation, Rothschild & Co Asset Management, april 2025

United States - Fed fund projection

en %, upper band



Source : Bloomberg, FOMC, Rothschild & Co Asset Management, april 2025

The Fed facing a complex challenge

The new trade policy will raise inflation, not only on imported goods but also on domestic prices, as input costs rise and demand increases on domestic products, whereas supply-chain disruptions will also translate into higher prices.

Yet, growth will also be negatively impacted. On the domestic economy, tariffs are a tax hike and, according to the Tax Foundation[4], the cumulative 20 percentage points rise in tariff rates this year would be the largest tax increase since the Revenue Act of 1968, which preceded the 1969-70 recession. Furthermore, the transmission of the tariff shock will likely be magnified by its negative effect on sentiment. Even before the shock on 2 April, the Conference Board and University of Michigan surveys, as well as the ISM indexes, showed that business and consumer confidence were down.

Although US imports will fall drastically, net trade will unlikely be a tailwind for growth. The magnitude and design of the Trump plan are likely to provoke widespread retaliations against US exports in key industries such as agriculture, technology and services. Breaking from its measured response to the previous 20 per cent increase in tariffs this year, China delivered a 34 percent tariff on all US imports alongside a broadening of export controls[1]. The European Union is also expected to retaliate, namely by limiting US firms from bidding for public contracts, and imposing restrictions on US technology firms and financial institutions. Canada initiated a WTO dispute regarding the auto duties, while Japan's Prime Minister Ishiba warned that tariffs would hamper his country's capacity to invest, a thinly disguised threat regarding future foreign direct investment in the US.

So far, investors seem to think that the growth effect will dominate, demonstrated by the increasing expectation that the Fed will cut rates swiftly to support the economy, in part due to its dual mandate of full employment and price stability. However, this rationale is incomplete in two important ways.

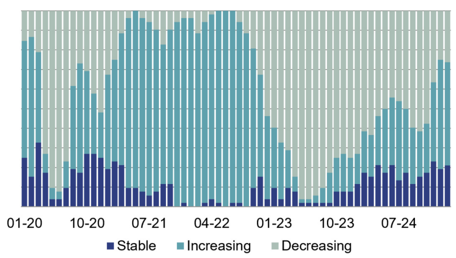
First, the slowdown in economic activity may not generate slack in the labour market as quickly as in the past. With illegal immigration collapsing, the labour force growing very slowly, and the Trump administration's decision to increase deportations significantly, very low monthly job gains could be enough to prevent the unemployment rate to increase significantly, at least in the short term.

Second, tariff-related price increases will be hard for the Fed to disregard if they drive up inflation expectations, in case they are not transitory. As of March, respondents in the University of Michigan's Surveys of Consumers expected long term inflation to average 4.1 per cent, the highest level in almost 35 years[5]. Incidentally, Fed Chair Powell made it clear that the Federal Open Market Committee will not take pre-emptive action, emphasising its obligation to keep longer-term inflation expectations well anchored, and to ensure that a one-time increase in the price level does not become an ongoing inflation problem.

Since the pandemic, the US economy has repeatedly proven its resilience, and defied recession forecasts. Still, the shocks are piling up, and the hardening trade war is sending global supply chains and trade into uncharted territory. The US's arbitrary tariffs increase stagflation and recession risks significantly, which explains most of the recent financial markets' turbulence. Expectations of more rate cuts have certainly risen, but inflation represents a significant constraint that will slow the Fed's reaction, which could dampen investors' hopes.

World - Change in global inflation

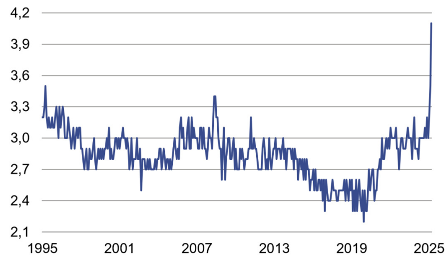
% of countries, 3m/3m



Source : OECD, Rothschild & Co Asset Management, april 2025

United States - LT inflation expectations

in %, University of Michigan survey



Source : Macrobond, Rothschild & Co Asset Management, april 2025

Performance of the indices and interest rate levels

	Price as of 31/03/2025	1 month % change	2025 % change
Equity markets			
CAC 40	7 791	-4.0%	5.6%
Euro Stoxx 50	5 248	-3.9%	7.2%
S&P 500	5 612	-5.8%	-4.6%
Nikkei 225	35 618	-4.1%	-10.7%
Currencies			
EUR/USD	1.08	4.3%	4.5%
EUR/JPY	162.21	3.8%	-0.4%

Interest rates	Level as of 31/03/2025	1 month change bp(1)	2025 change bp(1)
3 month			
Eurozone	2.30%	-10	-44
United States	4.29%	0	-2
10 years			
Eurozone	2.74%	33	37
United States	4.21%	0	-36

(1) Basis point.
Source: Bloomberg. data as of 31/03/2025. Performances in local currency.
Past performance is not a reliable indicator of future performance and is not constant over time. Index's performance is calculated on the basis of net dividend reinvested

Completed writing on 8 March 2025.

Check this document on our website

(1) Source: Bloomberg, April 2025
(2) Congressional Budget Office: The Accuracy of CBO's Budget Projections for Fiscal Year 2024
(3) Source: Tax Foundation and Yale Lab, April 2025.
(4) Tax Foundation is an international think tank based in Washington, D.C., that collects data and publishes studies on U.S. tax policies at federal and state levels.
(5) Source: University of Michigan, consumer surveys.

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