TRUMP'S TARIFFS ARE MAKING WAVES BUT MARKETS ARE STARTING TO IGNORE SHORT-TERM NOISE

This week markets are having to look past short-term news to discern a different long-term picture. The US imposed tariffs on trade with Mexico, Canada and China before swiftly granting an exemption for the US car industry. This was then extended to all goods which meet the terms of the US-Mexico-Canada Agreement on trade. Based on previous experience, it would be no surprise if temporary exemptions become permanent and more industries get a carve out. Markets have been volatile but currency markets, at least, now appear to be looking past short-term distractions.

Similarly, the rush to increase defence spending in Europe is significant, but the reforms being pushed by Ursula von der Leyen and Friedrich Merz may have more significant long-term consequences. If agreement can be found for joint borrowing for joint defence projects, there will surely be scope for this to be considered for other large scale shared endeavours. Meanwhile, the German proposal to exempt defence spending from government debt limits could free up considerable financial firepower to tackle other areas, such as infrastructure, which need more investment.

THE MARKETS THIS WEEK

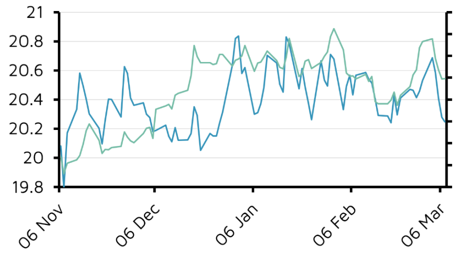
FTSE 100	S&P 500	Nikkei 225	STOXX 600	Hang Seng	US 10 Yr	UK 10 Yr	Brent Crude	Gold	Copper	GBP USD
-1.35%	-1.78%	-0.74%	-0.50%	+5.26%	+0.01%	+0.16%	-3.37%	-0.63%	+5.23%	+2.54%

US: TRUMP'S ON AND OFF APPROACH TO TARIFFS DRIVES VOLATILITY

The US followed through on threats to impose 25% tariffs on goods imported from Canada and Mexico. In addition, the US introduced a 10% tariff on Canadian energy and a further 10% tariff on Chinese imports. In his State of the Union address to Congress this week, President Trump promised new tariffs on imports from the EU, South Korea, Brazil and India from next month.

US equities experienced considerable volatility as they fell sharply on the day tariffs came into effect. They staged a recovery the following day but since resumed their decline and are set to post a loss for the week. Market volatility was increased by the exemption of imports by US car makers, which were granted a one month deferral. This helped companies like Ford and General Motors to buck the down trend. The confirmation of these tariffs saw the US dollar initially strengthen against the Mexican peso and Canadian dollar. However, it reversed this rise and the US dollar continued its recent decline against the euro and pound.

US Dollar Exchange Rate Against the Mexican Peso (LHS) and Canadian Dollar (RHS)

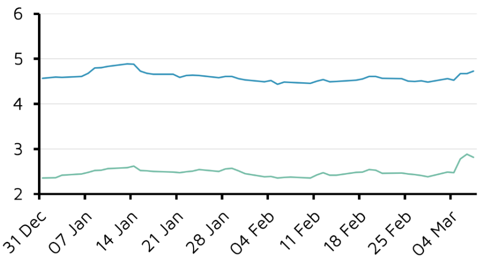


EUROPE: ECB CUTS RATES AS GERMAN BOND YIELDS SOAR

The European Central Bank cut interest rates to 2.5%. The 0.25 percentage point reduction was expected but the bank warned the rate of future cuts is likely to slow as it reduced its forecast for Eurozone growth from 1.1% to 0.9% this year. The rate cut follows European CPI inflation slowing to 2.4% in February. The potential for slower rate cuts provided a further boost to the euro as it added to recent gains against the dollar.

Meanwhile, German government bonds sold off heavily as the incoming German chancellor Friedrich Merz proposed sweeping reforms to the country's strict government borrowing limits. As well as removing the debt brake, which limit the speed at which government borrowing can be increased, Merz announced plans for a new 500bn euro infrastructure fund. This raised hopes that German economic growth will be revived. However, it caused a big sell-off in German government bonds as the yield on 10-year Bunds jumped 0.5% to 2.89% and closed some of the yield premium to other developed government debt.

Yield on 10-Year UK Gilts and 10-Year German Bunds (%)

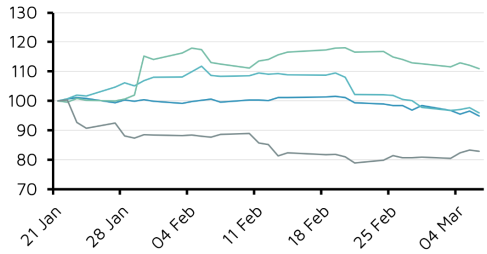


EQUITIES: TRUMP'S POLICIES CONTINUE TO DRIVE MARKETS

Defence stocks gained again as European governments rush to fill the void left by the US reducing its security commitments. European Commission president Ursula von der Leyen proposed an extra 800bn euros of borrowing to fund defence spending as new German chancellor Friedrich Merz suggested that EU limits on government borrowing should allow unlimited spending on defence. This led to a further rally in defence stocks. European satellite operator Eutelsat gained more than 400% as investors consider whether it can step in if US firm Starlink ends internet coverage for Ukraine's military.

US management consultancies are also feeling the effect of new policies from the White House. The Trump administration has rapidly cancelled or curtailed consultancy contracts since Donald Trump took office in January. Although shares in Palantir have soared in value since last November, shares in consultancies including Accenture, IBM, Leidos and Booz Allen Hamilton have fallen as their government contracts come under threat.

Performance of Accenture, IBM and Leidos v S&P 500 Since Trump's Inauguration (% change)



Data sourced from Investing.com.