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Navigating trade war turbulence

CROSS ASSET INVESTMENT STRATEGY

APRIL 2025 • Document for professional investors only

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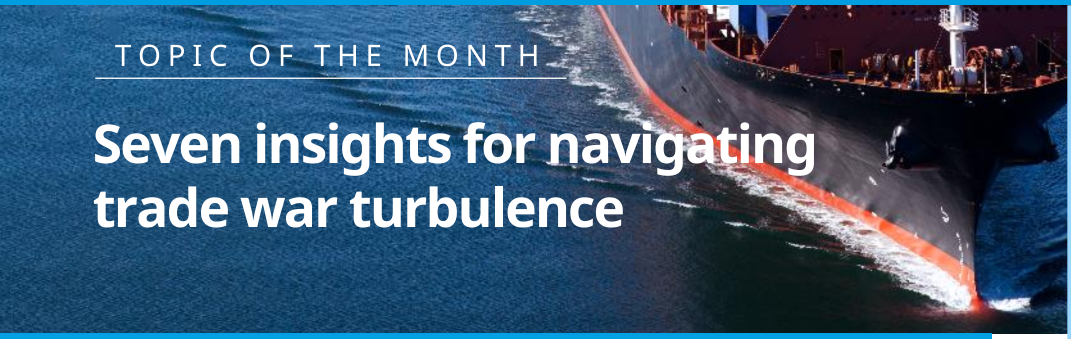
"All eyes are now on the earnings reporting season, as profits will be paramount. Margins are under pressure from rising input costs, and revenues are softening amid weaker demand. A profit recession may materialise ahead of, or even without, an economic recession."

MONICA DEFEND
HEAD OF AMUNDI INVESTMENT INSTITUTE

"In this trade war environment, we expect market rotations to continue and volatility to remain high. We favour European bonds, and a diversified stance in equities and gold."

VINCENT MORTIER
GROUP CHIEF INVESTMENT OFFICER



TOPIC OF THE MONTH

Seven insights for navigating trade war turbulence

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KEY TAKEAWAYS

As the global economy faces significant disruptions due to ongoing trade wars and tariffs, we believe it is crucial for investors to adapt their strategies to navigate this volatile landscape.

While the situation is too fluid to predict accurate economic patterns, we believe a profit recession could arise due to higher costs, lower demand, and increased uncertainty. Although markets have focused on growth damage from tariffs, inflation risks are also rising.

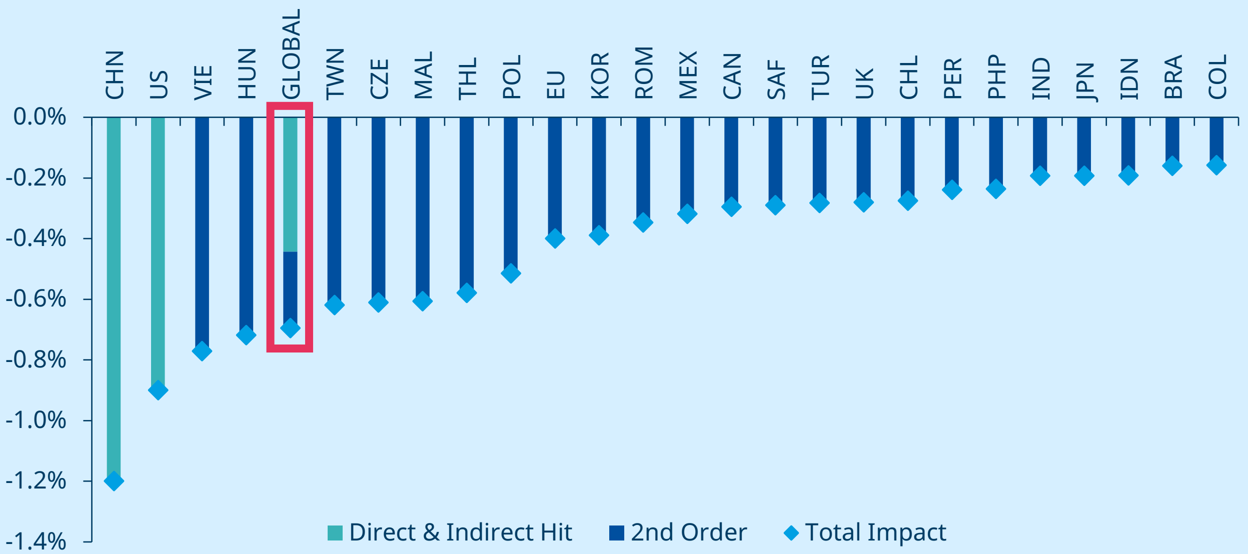
We have entered an era of structural shifts that will drive investment opportunities. Overall, we favour European fixed income and a highly diversified equity stance, while also continuing to balance the overall allocation with hedges and gold.

1. Balance risks in a world with no economic winners

We believe the severe disruption of the free trade model will have immediate and profound consequences, affecting all economies involved. The extent of this 'detoxing medicine' and the resulting retaliation will impact economic growth and hurt corporate profits.

Therefore, a profit recession could materialise ahead of, or even without, an economic recession, resulting in continued higher volatility. The ongoing uncertainty about whether tariffs will be imposed or paused is not changing the overall direction; instead, it is likely to increase volatility in financial flows.

Estimated GDP impact from current tariffs as of April 9th



Source: Amundi Investment Institute, Bloomberg, S&P Model. As of 10 April 2025.

This could result in more frontloading of orders before tariffs take effect, while also causing a halt in investment and capital expenditure plans due to the extreme uncertainty ahead.

→ **Investment implication:** After the strong sell-off, a significant deterioration of the market environment is already priced in. While it's too early to add risk, it is also not time to panic into an extreme risk-off stance, as the situation remains fluid. Favour a balanced risk stance.

2. Reassess valuations

In our view, the recent market volatility has led to a rapid re-rating of US equities, with valuations dropping from a P/E ratio of 25 to 20. We believe that valuations remain high compared to historical averages. As we assess the landscape, we must consider the risk of further compression in multiples, particularly in sectors closely tied to growth, such as IT and communications.

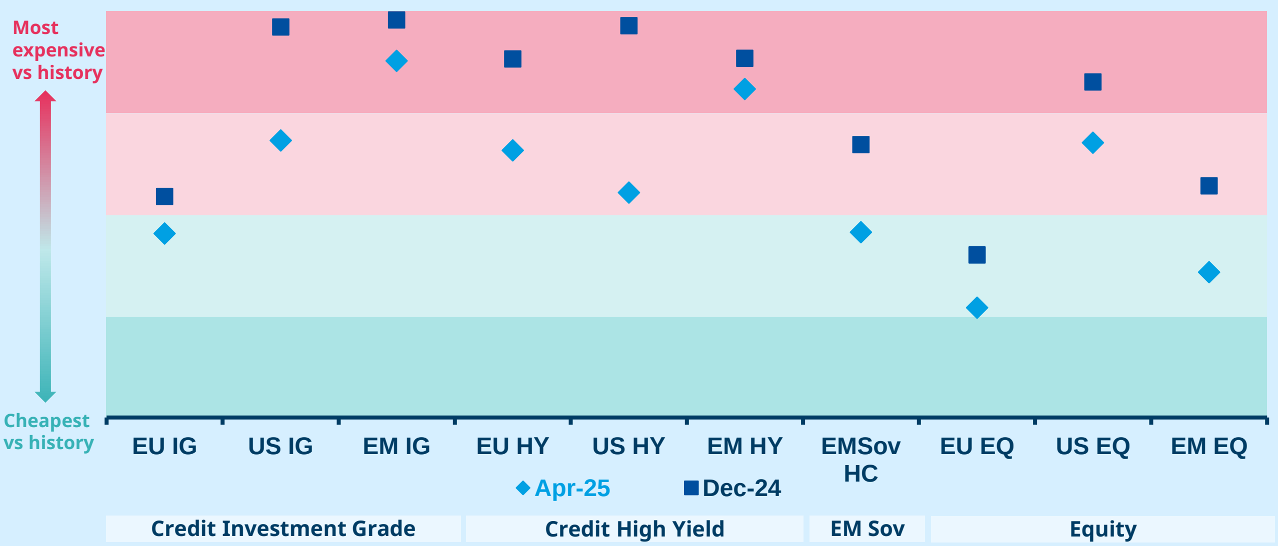
→ **Investment implication:** Stay cautious in areas where valuations continue to be tight such as US mega caps and tech stocks, look at opportunities in European equities (including small cap), be selective in Emerging Markets, such as the LatAm countries less impacted by tariffs, and sectors/names where valuations have become more appealing.

3. Seek opportunities arising from new trade alliances

We believe that the ongoing trade tensions will prompt countries to rewire their economic relationships, seeking new alliances. This is not a new phenomenon; tariffs have been a part of the landscape for some time. For instance, Europe has successfully closed eight trade deals, while China has secured nine.

→ **Investment implication:** We see this as an opportunity for investors to identify regions and sectors that may benefit from these shifts, particularly as China looks to Eastern Europe for manufacturing.

Valuations reset since the start of the year (historic percentiles since 1998)



Source: Amundi Investment Institute, Bloomberg, Datastream, latest monthly data as of 4 April 2025. Apr-25 refers to 4 April 2025; Dec-24 refers to 8 January 2025. EU IG, US IG, EM IG, EU HY, US HY, EM HY are ICE BofA corporate bond indices. IG: investment grade. HY: high yield. EM Sov HC: JP Morgan EMBI Global Diversified. EU EQ, US EQ, EM EQ are MSCI indices for equity markets. All indices refer to a specific region (EU: Europe, US: United States, EM: emerging markets. Analysis is based on spreads for bond indices and on twelve-month forward PE ratio for equity indices. Valuation are in historic percentile since 1998. Cheapest means is in the first quartile, Most expensive is in the fourth quartile.

4. Focus on European fixed-income opportunities

In our view, the current environment presents a compelling case for European government and investment-grade corporate bonds (particularly banks) over US bonds. The volatility in the bond markets, with the 10-year UST fluctuating from 4.80% to 4%, indicates a market pricing in a higher probability of recession. We believe that the ECB is in a better position than the Fed, focusing primarily on growth impacts from trade tensions, while inflation should be less of a concern.

→ **Investment implication:** Seek opportunities in the Euro aggregate bond space, play duration tactically.

5. Prepare for inflation pressures

We believe that markets may be underestimating long-term inflation pressures. The initial market reactions have focused on growth, but we see a risk that inflation could become a more significant concern.

→ **Investment implication:** Investors should consider strategies to protect their portfolios against inflation, such as incorporating commodities or inflation-linked securities, especially as breakeven rates suggest a need for inflation protection.

6. Navigate equity volatility with a diversified stance

In the current trade war environment, we anticipate ongoing market rotations and sustained high volatility. We believe that diversification is more crucial than ever, especially as the dollar loses its traditional role as a safe haven. Selection is also increasingly important to assess which sectors and businesses are best positioned to navigate rising costs from tariffs and relocation trends.

→ **Investment implication:** We balance exposure between cyclical and defensive sectors. Small-cap stocks, which have historically traded at a premium to large caps, are now available at significant discounts. We believe that their domestic focus makes them more resilient to tariff impacts, particularly in Europe and Japan.

7. Keep a strong focus on risk management, include gold and hedges to navigate uncertainty

We believe that maintaining agility in portfolio management is vital as we navigate these turbulent waters. With earnings expectations likely to be revised downwards, investors should be prepared to adjust their exposure based on evolving market conditions.

→ **Investment implication:** Hedging strategies, including the use of gold and derivatives, can help investors to manage risk effectively.

Tariffs will likely hurt the dollar

The typical USD negative correlation with equities has been tested since ‘Liberation Day,’ confirming one of our key assumptions for the outlook of FX. Tariffs may be bad for the global economy but given the huge accumulation of USD assets since the Great Financial Crisis, repatriation flows (or higher hedge ratios) will likely hurt the USD.

The growth-inflation mix is not yet conducive of an extremely dovish Fed, but holding rates steady in the short-term could still suggest deeper cuts ahead. A bull-steepening of the US yield-curve has historically translated into a lower USD, and there is room to correct, given the still solid premium to fundamentals.

Despite this, the USD remains one of the most expensive currencies globally. Risks to global growth suggest that it is premature to sell the USD across the board. For now, 'core currencies' in the G10, particularly the euro (EUR) and Japanese yen (JPY), appear to be safer options. In contrast, cyclical currencies are not yet out of the woods.

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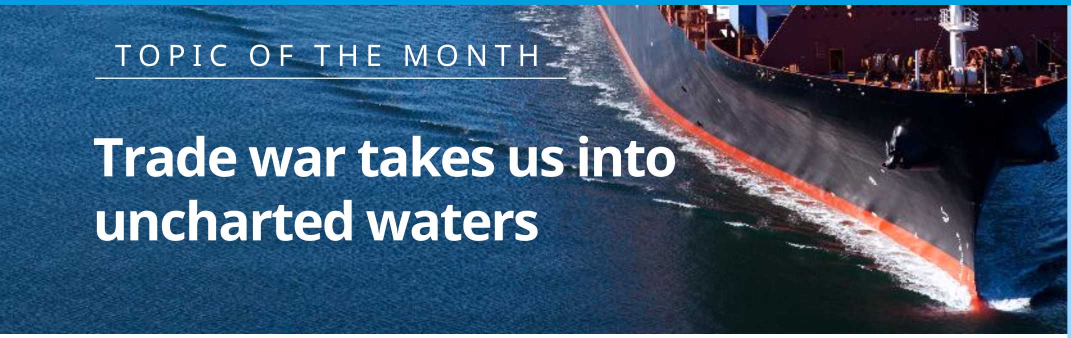

TOPIC OF THE MONTH

Trade war takes us into uncharted waters

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A significant increase in protectionism and uncertainty

In the midst of still extreme uncertainty and the unprecedented high tariffs imposed by the US, constructing any medium-term scenario is fraught with equally high uncertainty. Even with the 90-day suspension of reciprocal tariffs, uncertainty will be high, including on domestic economic policies in the US. As a result, US growth will be marked down substantially.

Not a good outlook for US growth

The impact will be widespread, and will primarily result in lower global growth, especially for the US's largest trading partners. But the growth hit will be strongest in the US and longer lasting. While inflation will also be higher – expectations of inflation over the next two years have already risen markedly – we would expect weaker growth to weigh on inflation. The impact on growth will be more adverse and longer lasting. US growth is likely to come down to around 1 percent his year (from close to 3 percent last year), effectively stagnating this year, and with only a marginal pick up next year. Inflation could stay above 3 percent for a while. Inflation will also lead to a decline in real incomes with no offset this year from a neutral fiscal impulse.

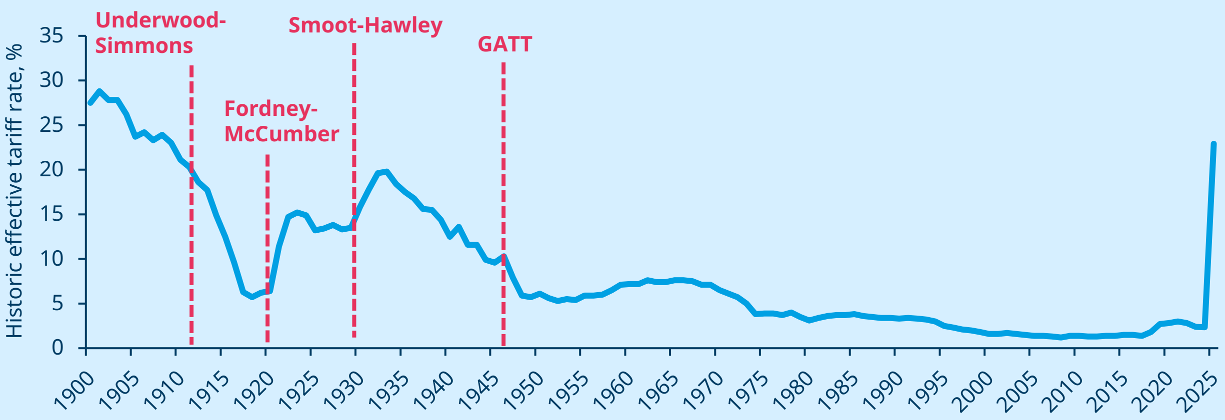
The Fed's near-term task will be complicated by tariffs raising inflation, but the weak growth backdrop should enable it to cut rates at least three times before the end of the year.

Stronger policy support elsewhere

China and the EU, will be incentivised to offer more macro policy support. China will likely implement a bigger domestic policy stimulus. And in Europe, fiscal consolidation efforts will be delayed, while the ECB could become more proactive as the inflation outlook continues to be benign and growth could fall well below 1 percent this year. We would expect ECB policy rate at 1.75 percent or lower by end year.

"With almost all countries subject to a significant increase in tariffs, especially the US's largest trading partners, the impact will primarily be lower global growth."

US tariff rates mark unprecedented times for the 21st century



Source: Amundi Investment Institute, US Census Bureau, Tax Foundation. Data is as of April 2025.

Main and alternative scenarios

	Probability 70% **MAIN SCENARIO** Growth at risk	Probability 25% **DOWNSIDE SCENARIO** High protectionism here to stay	Probability 5% **UPSIDE SCENARIO** Return of international cooperation and tech driven productivity change
GEOPOLITICS	▪ Tariffs stabilise around 20% in US, with limited reprisals elsewhere. ▪ Slow onshoring of supply chains. ▪ Ukraine-Russia: ongoing fighting. ▪ Middle East: talks and conflicts likely. ▪ China-US: relations remain tense. ▪ US-Europe: relations strained.	▪ A more permanent breakdown in advanced country cooperation. ▪ Countries forced to choose between the US and China. ▪ Global trade begins to decline.	▪ Geopolitical risk subsides. ▪ Global trade flows change but continue, fostering balanced growth and prosperity.
INFLATION & POLICY MIX	▪ Fed cuts three times despite US stagflation risk. ▪ ECB cuts rates to 1.75%. ▪ Most EM CBs at peak rates. China continues to ease. ▪ Divergent fiscal policies: US mild tax cuts and mild spending cuts. EU defence spending halts consolidation; China expands.	▪ Liquidity risks and bankruptcies increase. A crisis event forces central banks to cut even though inflation remains high. ▪ Global capital flows decline. ▪ High fiscal deficits increase term premia and funding costs.	▪ Cooperation to reduce protectionism stabilises markets. ▪ Inflation falls below targets, giving central banks room to cut to bolster growth.
GROWTH PATH	▪ Global growth hurt by tariffs, delaying return to potential growth ▪ EM still grows faster. ▪ India's growth potential revised up.	▪ Protectionism and reduced immigration into advanced economies lowers labour supply and growth. ▪ Lack of labour reform keeps growth potential low.	▪ Deregulation and new technologies (AI) boost growth. ▪ Protectionism subsides and industrial policies boost investment.
CLIMATE	▪ Climate change hampers growth and exacerbates stagflationary trends. ▪ Chinese dominance in critical minerals.	▪ Climate events increase, destroying capital.	▪ From zero to hero: geo-engineering, globally coordinated policies.

Risks to main scenario

LOW — Probability — HIGH

	10% **Buyers strike on US Treasuries**	15% **Geopolitical crisis with global spill-overs**	15% **Credit event provoked by market volatility**	20% **Reacceleration of DM inflation, due to trade/geopolitical tensions**
MARKET IMPACT	**Positive** for cash and gold. **Negative** for govies and expensive equities.	**Positive** for some DM govies, cash, gold, USD, volatility, defensive assets, and oil. **Negative** for credit, equities, and EM.	**Positive** for cash, gold and DM government bonds. **Negative** for risk assets.	**Positive** for TIPS, gold, commodity FX, and real assets. **Negative** for bonds, equities, DM FX, and EM assets.

Source: Amundi Investment Institute as of 7 April 2025. DM: developed markets. EM: emerging markets. CB: central banks. USD: US dollar. TIPS: Treasury inflation-protected securities. FX: foreign exchange markets.

EMERGING MARKETS FOCUS

EMERGING MARKETS FOCUS

Emerging Markets beyond the 90-day tariff pause

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President Trump has announced a 90-day pause on tariffs higher than 10%. However, in the meantime, he has further increased tariffs on China to 125%. In retaliation, China announced an 84% tariff on all US imports starting from April 10th. While the situation remains quite fluid, we will address some concerns from an economic standpoint regarding growth and inflation.

Despite this pause, the final effective tariff for the US is unlikely to change dramatically from previously anticipated levels, largely due to provocations from China. As a result, the global economic outlook continues to trend downward, with global inflation pressures likely to be further exacerbated by the recent US-China trade war escalation.

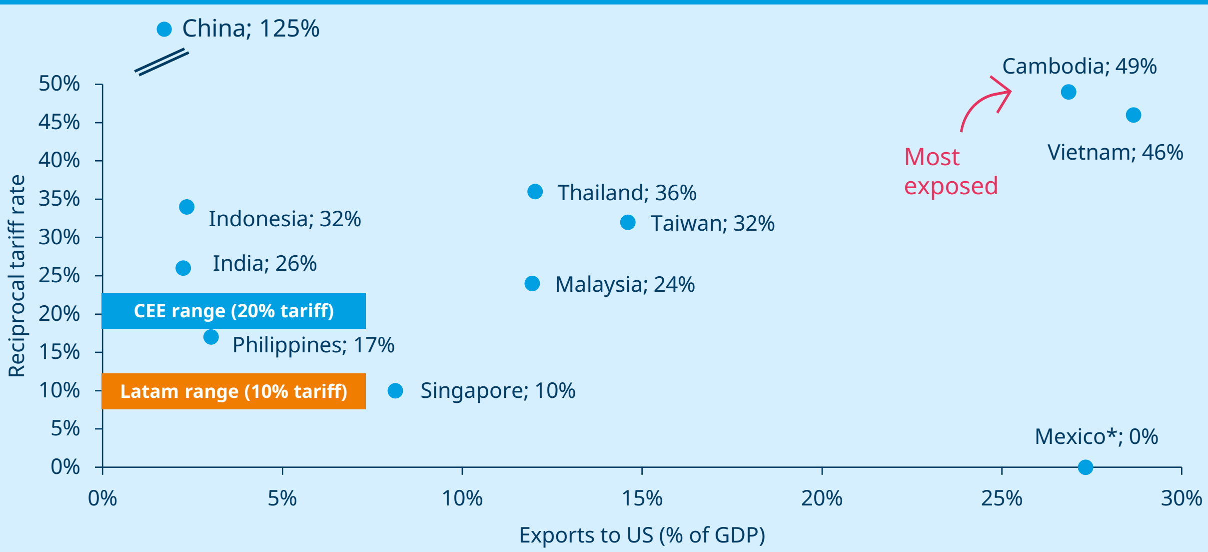
The announced tariffs should hit Asia the hardest, a predictable outcome given the region's high level of integration in the production and export of goods to the US, which has resulted in a significant external surplus. The highest rates were initially levied on small countries such as Vietnam, Cambodia, Laos, and Sri Lanka, but soon escalated to China following its retaliation.

For Central and Eastern Europe (CEE), the impact is more indirect and linked to the perspective of tariffs for Europe and Germany, as well as any macroeconomic deterioration there. The most vulnerable countries are Hungary and the Czech Republic, as they are highly integrated into the Germany-led EU automotive supply chain. By contrast, Romania and Poland appear more shielded, considering their less direct trade linkages.

"The trade war's impact will be profound for Asian countries, while some Central and Eastern European and Latin American countries appear more insulated."

'Reciprocal' tariff vs Exports to US effective and threatened as of April 10th

'Reciprocal' tariffs have been put on hold for 90 days starting from April 9th except for China for which the total tariff is 145%. During this pause, all other countries will face a 10% tariff.



Source: Amundi Investment Institute, Bloomberg, White House, Annex I: Tariff Rate. Data is as of 9 April 2024. *Total tariff rate for China. Mexico is under the UCSMA agreement not affected by reciprocal tariffs.

More surprisingly, South Africa's tariff was initially set at 30% despite its existing trade agreement with the United States under the African Growth and Opportunity Act (AGOA). This casts doubts on AGOA's future and sparked uncertainty about US-Africa trade relations more broadly.

Latin America saw the least impact from the announced tariffs, and key trading partners like Mexico were granted a temporary pause.

In addition, copper (a major export for countries such as Chile and Peru) was for the time being exempted from the tariff schedule.

The inflation outlook in EM is now even more uncertain, and highly dependent on several interrelated factors:

- A healthy currency devaluation would help to absorb the external shock, keeping some competitiveness at front of higher tariffs. With that resulting in higher imported inflation.
- Retaliation and temporary supply chain disruptions could result in temporary inflation spikes.
- On the opposite side: global oil prices are moderating, offering a counterbalance to tariff-driven inflation pressures; in addition, cheap Chinese products need to find other destinations than the US, therefore, amplifying the disinflationary trend.

What is the market impact?

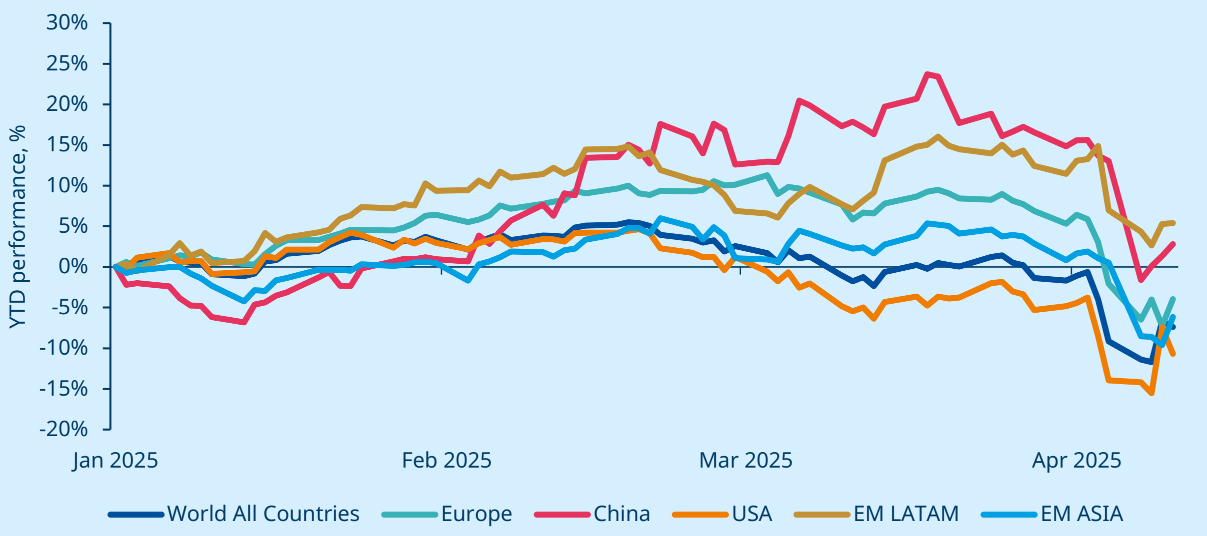
The reset of equity valuations across emerging markets allows for an improved upside potential. However, our earnings per share forecasts at 12 months, which had already been positioned below consensus, are now at risk of further downward reduction due to a more tepid export outlook.

Asia ex-China stands to benefit the most from current valuations: **India and the Philippines may emerge as relative winners thanks to their lower vulnerability to tariffs and supportive domestic demand trends**. Meanwhile, **the outlook remains neutral/constructive for LatAm and CEEMEA at a regional level; Mexico continues to be favoured,** supported by its tariff pause.

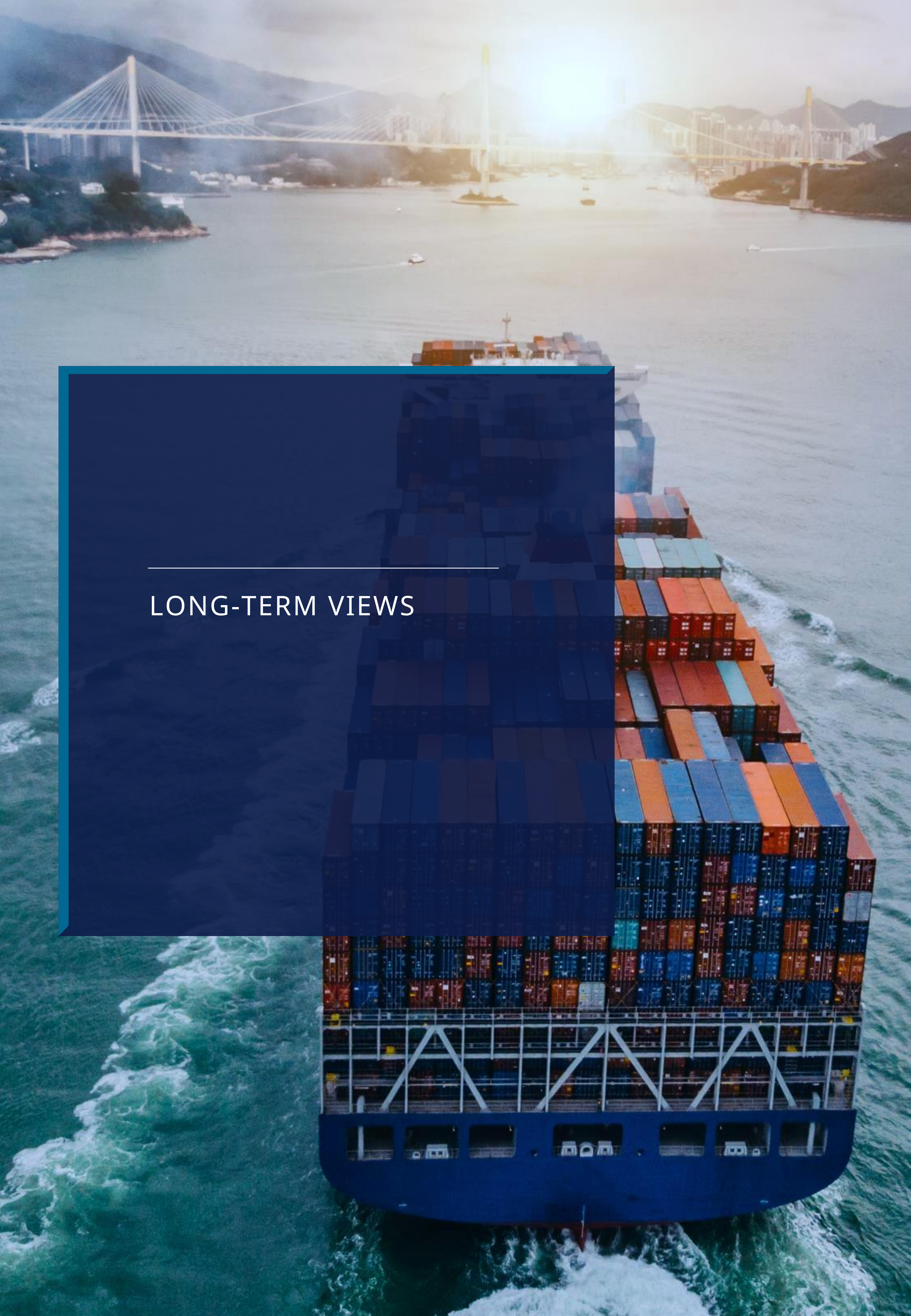
In fixed income, our ongoing call for a weaker USD supports a selective and tactical allocation across the EM FX universe. We have marginally become more constructive on the Indian rupee offering high carry and less volatile dynamics.

Local debt performance continues to hinge on the path of the Fed and the reaction of EM central banks. US yields' term premia introduce an element of risk. In hard currency debt, spreads widened across the board in the wake of the tariff announcements, affecting both investment-grade and high-yield segments. However, we remain constructive and notably, for the first time in a while, we anticipate some value in EM IG as spreads are expected to tighten.

In equities, LatAm most resilient. Second-round effect: impact due to weaker trade dynamics



Source: Amundi Investment Institute, Bloomberg. Data as of 10 Aprile 2025. MSCI price Indices in local currencies.
Past performance is no guarantee of future results.



LONG-TERM VIEWS

LONG-TERM VIEWS

The uncertain reality of tariffs

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President Trump has highlighted the benefits of 'Liberation Day' tariffs, which include: 1) rebalancing trade, 2) reindustrialising America, and 3) reducing fiscal deficits by taxing those engaged in 'unfair' trade practices. While these issues are undoubtedly significant, it remains uncertain whether tariffs are the appropriate mechanism to address them. In order to ascertain the effectiveness of Trump's tariff policy, we examine the current landscape and the possible implications for financial markets.

Trade imbalances and tariffs

The relationship between trade balances and tariff rates is not straightforward. If more protectionist countries were to benefit from tariffs, one would expect to observe a positive correlation between the tariffs a country imposes and its trade balances. However, this is not the case. According to economic theory, the size of trade imbalances is more closely associated with the disparity between domestic savings and investment. Unless tariffs can significantly alter the savings and investment behaviour of Americans, **the prevailing economic theory—supported by empirical evidence—indicates that the likelihood of President Trump enacting a meaningful change to the US's trade positions is low.**

> *"The trade war is triggering a shift that could alter the current international framework and call into question the US dollar and US Treasury's safe-haven status."*

Structural changes needed for manufacturing revival

Structural changes, rather than tariffs, are essential for revitalising American manufacturing. The decline in the manufacturing share of GDP has coincided with the growth of the services sector (such as finance and technology) and rising costs for American workers. With unit labour costs rising substantially over time, many firms have relocated to remain competitive. The critical question is whether tariffs can revive manufacturing competitiveness and spur a needed resource re-allocation from Wall Street and Silicon Valley back to the rust-belt states. Scepticism abounds.

Tariffs as a revenue generator

For tariffs to effectively generate revenue, they must be **sustained over time and primarily paid by foreign entities**. But if the implementation lacks flexibility, their effectiveness as a negotiation tool diminishes. Moreover, **the stagflationary pressure they create could heighten the risk of economic downturns and inflation**, exacerbating the US government's financial challenges.

The question of who bears the cost is important too. While the US President hopes others will shoulder this burden, historic examples show that US consumers have largely absorbed the costs of tariffs. This concern has contributed to the recent decline in consumer confidence.

The uncertain reality of tariffs

In summary, the reality of what tariffs can achieve is highly uncertain. While we doubt their ability to precipitate the substantial economic transformation necessary to fulfil the President's objectives, there is a possibility that they will lead to significant rebalancing in trade.

"Consequently, globalisation may take a backseat, as the world's two largest trading nations simultaneously turn inward."

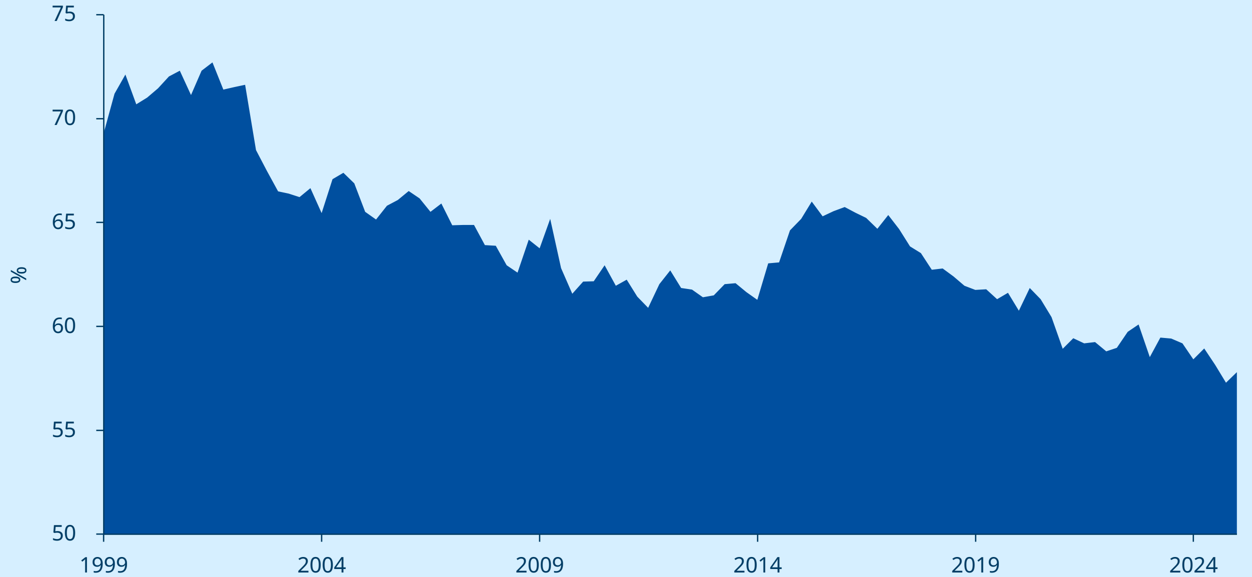
A rewiring of the global trade system

The global trade system could undergo significant changes if the largest deficit-running country is able to rebalance trade. If there are no substitute buyers of global products, the rest of the world will be compelled to adjust their positions. **A balanced trade position for the US does not necessarily imply a reduction in transactions with the rest of the world**; rather, it implies that imports and exports will become more equal. However, if Trump is successful in reshoring manufacturing to produce goods domestically, this could lead to a more self-sufficient US economy with a diminished reliance on imports. **Additionally, China is also attempting to reduce its export dependence by stimulating domestic demand for its own products.** Consequently, globalisation may take a backseat, as the world's two largest trading nations simultaneously turn inward.

The implications for financial markets are significant, particularly for the US dollar and the safe haven status of US Treasuries

Chronic current account deficits have allowed the US to "export" its currency, establishing the dollar as the global reserve currency. However, rebalancing trade accounts may undermine demand for the dollar and disrupt its circulation, potentially eroding its reserve status over time. While there is no immediate threat to the dollar's dominance, increasing competition from hard and digital currencies could accelerate this decline.

US dollar share of foreign reserves is declining



Source: Amundi Investment Institute, Bloomberg. Data as of 7 Aprile 2025. MSCI price Indices in local currencies.
Past performance is no guarantee of future results.

LONG-TERM VIEWS

Is gold still affordable? Yes

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Gold remains an island of stability in a sea of uncertainties

Uncertainty surged to a new level as the Trump administration launched the biggest **trade war** of at least a century with no immediate prospect of relief. Gold stands out as one of the few stable assets, bolstered by a declining dollar and fears of stagflation. Moreover, gold and other precious metals are likely to remain unaffected by tariffs.

Public deficits are another strong mid-term driver for gold, historically impacting markets when they fall below -4%. This threshold has already been breached by most developed market (DM) countries. The credibility of government plans to address these deficits, as well as the nature of spending (productive vs. non-productive), greatly influences investor confidence. Consequently, public finances and **political stability** are closely linked, and both are deteriorating in many DM countries. Gold, which backs only a fraction of these public liabilities, has substantial re-rating potential.

Current **geopolitical tensions** are broad and persistent enough to influence market dynamics and inflation trends. Tensions in the Middle East could lead to surging energy prices, while intensifying protectionism could affect imported producers' costs. Although a potential ceasefire in Ukraine could alleviate some tension, doubts about a lasting peace deal and increased EU defence spending are likely to maintain a long-term premium for gold.

In an effort to shield against currency fluctuations and geopolitical uncertainties, **central banks are expected to continue purchasing gold**, particularly those seeking to reduce their dependency on dollar transactions. Gold is also supported by its **physical fundamentals**. Weak growth in mining supply and rising extraction costs are contributing to higher spot prices, while jewellery demand is anticipated to increase in the medium-term, primarily driven by India.

"...public finances and political stability are closely linked, and both are deteriorating in many DM countries. Gold, which backs only a fraction of these public liabilities, has substantial re-rating potential."

Assessing valuation: Gold is not cheap, but not excessively expensive either

Gold continues to trade at all-time highs, even when adjusted for inflation. Determining whether gold remains affordable gets us back to its multiple roles: as a currency, a commodity, an investment asset, a luxury consumption good, and an industrial material.

As a commodity, gold appears expensive, particularly compared to other precious metals. It seems pricey relative to traditional macroeconomic drivers, but not against uncertainties, which makes it fairly priced as an investment asset. **As a consumer and industrial good, gold looks expensive** vs. income or wealth per capita (but will get support from surging demand in India) **but cheap vs. gold-user-intensive tech companies**.

Finally, **gold still looks very cheap as a currency**. The majority of public liabilities are not backed by tangible assets; instead, they rely on public and market trust, as well as the soundness of economic policies. In the US, for instance, every ounce of gold now backs $138,000 of public debt compared to less than $500 before the collapse of Bretton Woods. The re-rating potential of gold, as a currency, therefore, looks very significant.

Gold stands a$3200/oz milestone, which would clear the way for $3500/oz.

We expect gold volatility to increase as valuations rise and political dynamics – both domestic and international – remain unstable. However, we believe risks remain skewed to the upside. With gold at the $3200/oz milestone, we expect $3500/oz as the next target, as uncertainties remain high.

Potential for investors to increase their allocation of gold

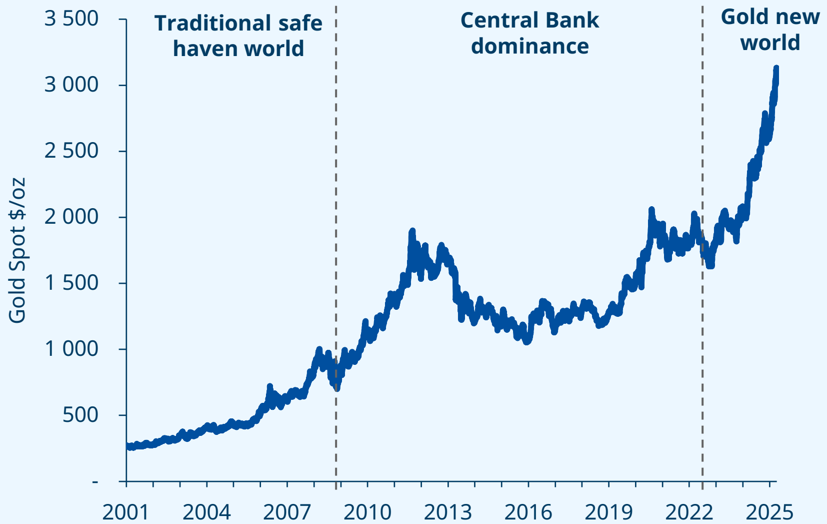
We estimate that global investors currently allocate about 2% of their portfolios to gold, amounting to approximately $4 trillion. This allocation is substantially below what portfolio optimisation techniques suggest. A potential increase to 3% could provide significant upside potential for gold prices.

Investors can gain exposure to gold through various means, including direct investment in gold bullion, gold ETFs, and shares in gold mining companies, which can serve as an appealing complementary option to traditional gold investments and remain cheap in relative terms.

The changing nature of Gold as a Strategic Asset in the 21st Century

Our models identify three distinct gold phases in the 21st century characterised by changing market dynamics and investor sentiment.

1. **2000-2008: Traditional Safe Haven.** During this period, gold maintained its classical role as a portfolio diversifier, a safe haven during recessions and periods of negative risk sentiment, and a resilient asset during geopolitical tensions.
2. **2009-2022: Central Bank's Dominance.** The implementation of unconventional monetary policies by central banks (primarily Quantitative Easing) fundamentally altered gold's trajectory. Gold was significantly repriced as a safe-haven asset. Increased demand was driven by concerns about potential failures of increasingly unconventional monetary policies, and market participants questioned the long-term credibility of the fiat currency system.
3. **2022-Present: Gold New World as Strategic Reserve Diversifier.** We now see a new environment for gold where demand will remain sustained by the appealing role of Gold as a stable asset increasingly in demand at a time where the dollar's centrality in the global monetary system is set to diminish. In this new world, we believe there is potential for gold to remain in demand and to rise further.



Drivers of Gold	Relevance in the gold new world
Rates & inflation	Medium
Growth	Medium
Debt	High
Risk sentiment	High
FX	High
Global Reserve Demand	High

Source: Amundi Investment Institute, Bloomberg. Data as of 7 April 2025.

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Amundi Investment Institute

In an increasing complex and changing world, investors need to better understand their environment and the evolution of investment practices in order to define their asset allocation and help construct their portfolios.

This environment spans across economic, financial, geopolitical, societal and environmental dimensions. To help meet this need, Amundi has created the Amundi Investment Institute. This independent research platform brings together Amundi's research, market strategy, investment themes and asset allocation advisory activities under one umbrella; the Amundi Investment Institute. Its aim is to produce and disseminate research and Thought Leadership publications which anticipate and innovate for the benefit of investment teams and clients alike.

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