First Citizens Wealth™

Making Sense

Basis Points | April 3, 2025

Markets React to New Tariff Turmoil

1. Steeper-Than-Expected Tariffs

The White House announced significantly steeper tariffs than the market consensus expected. The US levied an average tariff rate of 2.5% in 2024. **Following Wednesday's order, US imports will soon face an average tariff rate of over 20%, the highest at least since World War I.**[i] According to President Trump's executive order, the US will now charge a 10% baseline tariff on imports from all countries except Canada and Mexico. On top of this baseline, the US will charge additional import taxes on a country-by-country basis, which in some cases will be very high. For example, imports from China and Vietnam – which accounted for a combined 20% of all US imports last year – will now face tariffs of close to 50%. Exports from the European Union, which accounted for another 20% of US imports last year, faced average tariffs of 1% last year but will now be subject to a rate of over 20%.

2. Market Reaction

Markets initially reacted negatively with risk assets falling sharply. The incremental clarity is that the White House's announcement was substantially more aggressive than expected. But many important details for markets remain up in the air:

- **Which products?** Although the White House provided details on tariff rates for each country, it is far from clear what products will ultimately be subject to these new tariffs, and what will initially – and eventually – be exempted.
- **For how long?** The Administration has been clear they are approaching this conflict as the start of a negotiation. Thus, while some tariffs could be longer-lasting, others might change in the near-to-medium term (the immediate effect will likely still be felt unless the tariffs are called off entirely).
- **Will prices rise?** The longer-term effect on intermediate and consumer prices is extremely uncertain. Sharply higher tariffs act as a tax on imports, but how firms negotiate with sellers, maneuver supply chains, sacrifice margins, and raise final prices is impossible to estimate.
- **Will the US economy take a hit?** The negative effect on US domestic demand may be significant but again is virtually impossible to forecast with confidence. Estimates of the economic impact in many of today's news stories are the product of economic modeling efforts that rely heavily on questionable assumptions.
- **Will US trading partners retaliate?** Foreign economies will have to adapt, especially those whose exports constitute a substantial fraction of their economies. Some countries may even raise their own tariff rates in response, which could prompt further action from the White House.

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- **Legal challenge?** The White House invoked emergency powers to issue these orders. Because there is little precedent for such sweeping action in this realm, it is possible that yesterday's order could be challenged in federal court.

3. Looking Ahead

We expect market volatility will persist. We will be listening closely to management commentary to learn how firms plan to approach disrupted supply chains and higher import prices as first-quarter earnings season ramps up next week. In addition, we will be alert to companies' views on the tradeoff between lower margins, higher prices, and uncertain demand. Until this point, we have seen ample evidence that corporate leadership has taken a 'wait and see' approach, awaiting the rules of the road. Does the incremental clarity of this week's announcement change corporate perspective or does the higher-than-expected average tariff rate simply drive more C-suite uncertainty? Earnings season might shed some light on this question.

4. A Reminder…

In times of uncertainty and volatility, it is critical to remember the importance of a long-term, balanced approach to investing and the essential nature of a financial plan. Investors who sell risk assets in times of uncertainty might sometimes forego further sharp declines, but because timing markets is virtually impossible, it is all too common for them to miss the early days of the subsequent rally. That said, **2025 has already been an important reminder of the importance of balance across asset classes in portfolios.** As we stated in our 2025 Outlook: "Portfolio balance consistent with investors' goals and objectives is always important, but looking over the next 10 years, it might be even more essential than during the recent past."

i: Source: Historical Statistics of the United States, Treasury Department, Yale Budget Lab, Bloomberg