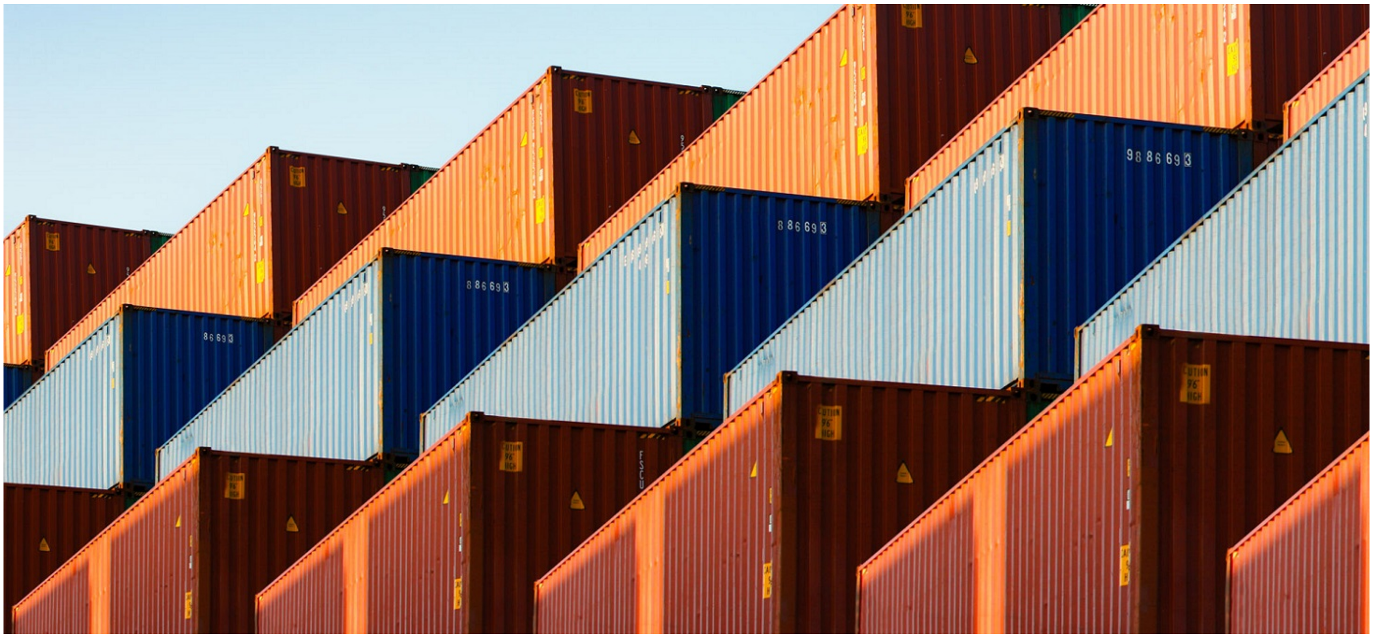

While CIO remain alert to new tariff risks, they keep their constructive stance on global equities, and on US stocks in particular. (UBS)

Tariff threats may trigger near-term market volatility

26 November 2024, 2:56 pm CET, written by UBS Editorial Team US Editorial Team

President-elect Donald Trump on Monday vowed to issue executive orders imposing new punitive tariffs on all imports from Mexico, Canada, and China on the first day of his presidency. Posting on social media, Trump said he would target Canada and Mexico with a 25% tariff, and China with a 10% tariff "above any additional tariffs," until the three countries address complaints over illegal migration and drug trafficking.

While details are still thin at this stage, we see several takeaways for global investors:

The anticipated transactional nature of tariff policy is taking shape. The use of tariffs to target non-trade issues confirms a transactional orientation from the Trump administration, in our view, aimed at gaining leverage and achieving outcomes over conforming to prior processes or norms. The president-elect's choice of Scott Bessent as Treasury secretary has been seen in the market as an anchor of stability and responsibility in the Trump cabinet. This does not suggest Bessent won't champion Trump's tariff strategy. In a recent Fox News oped, Bessent said tariffs could help "getting allies to spend more on their own defense, opening foreign markets to US exports, securing cooperation on ending illegal immigration and interdicting fentanyl trafficking, or deterring military aggression."

The timing and narrow focus of the latest threat suggest scope for negotiation. The current USMCA free trade agreement between the US, Canada, and Mexico is not technically up for review until 2026, but this latest tariff threat effectively marks the start of negotiations. Its national security framing offers legal cover, and both Mexico and Canada have already signaled plans to negotiate.

Stepping back, all three countries remain heavily reliant on each other economically, and hefty taxes on key US imports like crude oil or softwood lumber risk exacerbating US consumer inflation. We think lasting tariffs would likely take longer to craft, if they were meant to endure legal challenges. The narrow focus on drugs and migration issues suggests the Trump administration wants a path to resolution on these matters outside structural trade-oriented disputes in both North America and with China.

Tariff threats may trigger near-term market volatility, but the fundamental backdrop remains supportive. Since Trump's electoral win, markets have primarily focused on the incoming administration's pro-growth policies. Our base case for the year ahead is for still-solid US growth supported by deregulation and improved business confidence, which can more than offset the impact of selective tariffs. This early proposal from President-elect Trump may prompt investors to consider risk outcomes for trade, including the potential for large, blanket tariffs imposed on imports from multiple countries. At a minimum, a return to US diplomacy by social media posts and tariffs suggests a new period of heightened cross-asset volatility may be ahead.

While we remain alert to new tariff risks, we keep our constructive stance on global equities, and on US stocks in particular. Within the US, the technology, utilities, and financial sectors are among those we see as Attractive. We take the fairly muted reaction in China stocks on Tuesday as a reflection of the market's focus on the core tariff threat—the 60% headline figure—and we continue to recommend a defensive position within China equities. US dollar strength may continue in the short term, with tariffs, tax cuts, and deregulation potentially supporting the currency. But we think the dollar is overvalued, and suggest investors use near-term strength to decrease exposure. We continue to advocate for adding portfolio hedges like gold, and favor diversification into alternatives and other less-correlated assets.

To read more on potential tariff scenarios and their economic implications, please see our recent *Global Risk Radar,* **"What could Trump 2.0 mean for global trade?"** (published 19 November 2024).

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