Ostrum
ASSET MANAGEMENT

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Market views and strategy

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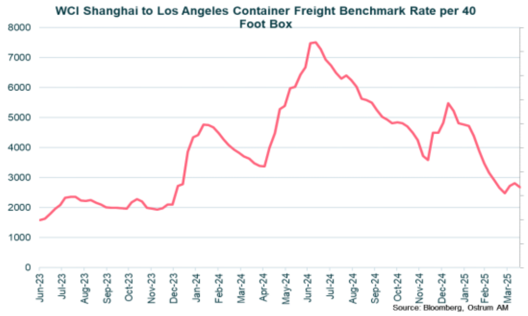
Topic of the week: The EU under the test of the trade war
by Aline Goupil-Raguénès

- Despite the suspension of reciprocal tariffs, the average effective tariff rate in the United States is at its highest since 1901, at 28%, primarily due to the massive tariffs imposed on Chinese products;
- European goods are subject to a 10% tariff, which is ten times higher than the rates that previously applied. In addition, there are 25% tariffs on cars, steel, and aluminum. Other tariffs could be announced soon, particularly on semiconductors and pharmaceutical products;
- Given the prohibitive tariffs between China and the United States, the EU is at risk of facing a significant influx of highly competitive Chinese products. The EU has indicated that it will take measures to limit this;
- Beyond forming partnerships with other countries, it is essential for the EU to strengthen the European single market, which still faces significant tariff barriers. These are estimated to be equivalent to tariffs of 44% on goods and 110% on services, according to the IMF;
- Given that European countries primarily trade among themselves, removing these barriers to intra-zone trade would significantly enhance productivity and growth in the EU.

Market review: Coming up for Air
by Axel Botte

- U.S. retail sales bounce in April;
- Euro area: ECB cuts rates by 25 bps as expected;
- Calm back in U.S. Treasury bond market: T-note around 4.30%;
- Equities: equity rebound in Europe despite the technology sector's underperformance.

Chart of the week



Tariffs, in effect since Mid-March, are already weighing on global trade. Container rates are down since February. But in a further escalation to the trade war, the Trump administration plans to impose fees on Chinese-built and -owned ships docking in the US, as well as non-Chinese shipbuilders, to support the US shipbuilding industry.

The fees would be based on the volume of goods carried, with Chinese vessels to be assessed $50 per net ton after six months, increasing incrementally over three years.

Figure of the week

7

Last week, the ECB proceeded with its 7th rate cut since June 2024. The deposit rate was brought down to 2.25 %.
Source: Bloomberg

Topic of the week

The EU Under the Test of the Trade War

Despite the 90-day suspension of reciprocal tariffs, EU merchandise exports are facing a sharp increase in U.S. tariffs. These could affect new products, such as semiconductors and pharmaceuticals, and potentially rise from 10% to 20% in early July if negotiations fail. Ireland is by far the most exposed economy, followed by Belgium, the Netherlands, Germany, and Italy.

Despite the suspension of reciprocal tariffs, the average U.S. tariffs are at their highest levels since 1901.

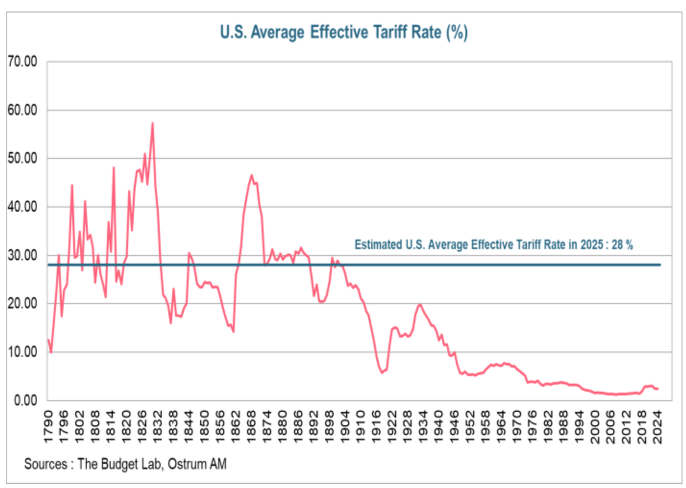
The debacle in the U.S. financial markets, triggered by the imposition of reciprocal tariffs against all trading partners, led Donald Trump to make a dramatic about-face by announcing their suspension for 90 days, just after they had been implemented. Basic tariffs of 10% apply to American imports from nearly all countries, with Russia, North Korea, and Cuba being notable exceptions. There are exemptions for chips, copper, wood, pharmaceuticals, bullion, energy, and minerals not found in the United States.

China receives special treatment... Reciprocal tariffs persist, and U.S. tariffs reach a total of 145%.

China receives special treatment... Given that it retaliated promptly against the increases in U.S. tariffs, reciprocal tariffs remain on Chinese goods and have even been raised to 125%. Taking into account the previous rate of 20%, U.S. tariffs on imports of Chinese goods now total 145%! China responded immediately with tariffs that now reach 125% on imports from the United States. These prohibitive tariffs will result in a near halt of bilateral trade between China and the United States.

The average effective tariff rate in the United States is 28%, the highest since 1901.

Thus, despite the 90-day suspension of reciprocal tariffs, with the exception of China, and the exemption of certain products such as smartphones, tablets, and computers (announced on April 11), the average effective U.S. tariff rate remains at its highest level since 1901. It has significantly increased since Donald Trump returned to the White House due to the imposition of 25% tariffs on steel and aluminum imports, automobiles, imports from Canada and Mexico, 10% base tariffs on all countries, and 145% tariffs on China. Sanctions against Venezuela have also been extended: 25% taxes apply to all third countries importing oil from Venezuela. The average effective U.S. tariff rate is thus estimated to be 28%, according to The Budget Lab's estimate from April 15.



Threat of new tariff increases

On May 3, a 25% tariff will be applied to automotive parts, and this may be followed by tariffs on semiconductors and pharmaceutical products.

The United States is expected to announce new tariffs in the coming weeks/months.

This will begin on May 3: **automotive parts** will be subject to an additional 25% tariff.

Taxes are expected to be imposed on **Chinese shipowners and operators docking in U.S. ports**. The amount of the fee will depend on the vessel's tonnage. After a period of 180 days, a fee of $50 per net ton will be imposed, which will gradually increase by $30 over a period of three years, according to the proposal from the Department of Commerce on April 17. The taxes will be applied based on the number of trips to the United States and not on the number of port calls to avoid penalizing smaller U.S. ports.

The U.S. administration has also launched investigations to determine whether certain imports pose a threat to the national security of the United States. The findings could lead to an increase in tariffs on: **copper, wood and lumber, pharmaceuticals and pharmaceutical ingredients, semiconductors and semiconductor manufacturing equipment, critical minerals, and rare earth elements.**

On February 21, the White House also issued a memorandum expressing concern about the treatment of American digital companies abroad, particularly in the EU. The trade representative is to review the **digital services taxes imposed by Austria, France, Italy, Spain, Turkey, and the United Kingdom**.

Finally, in early July, **reciprocal tariffs could be reinstated** if negotiations between the U.S. and various countries fail.

In Europe, Ireland is the most exposed

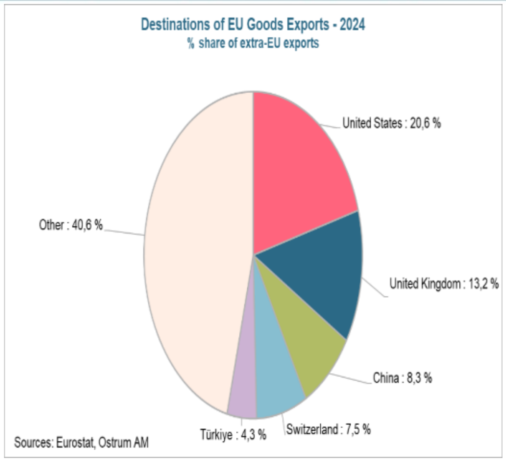
Tenfold increase in U.S. tariffs on European goods

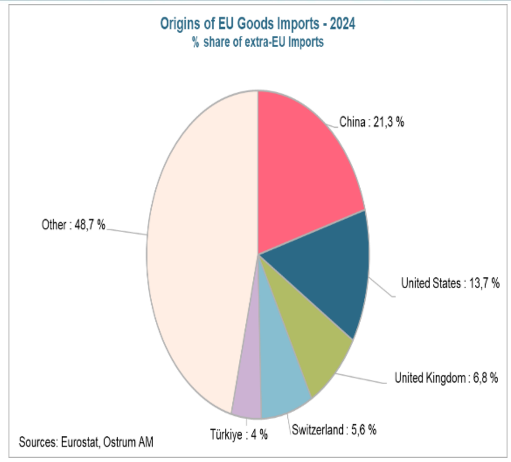
The EU is facing a basic tariff of 10% on goods exports to the United States.

European goods imported by the United States have been subject to a base tariff of 10% since April 5. This represents a tenfold increase compared to the tariffs that were in place before Donald Trump's return to the White House, which were around 1% according to the European Commission. This will inevitably have consequences for bilateral trade. These consequences could be even more significant if these tariffs are increased by reciprocal tariffs to 20% in early July.

The United States is the top destination for EU exports

The United States is the European Union's top trading partner. It is the leading destination for EU exports, accounting for 20.6% of extra-EU exports in 2024, ahead of the United Kingdom and China. In terms of imports, the United States ranks second, with 13.7% of extra-EU imports, behind China (21.3%).



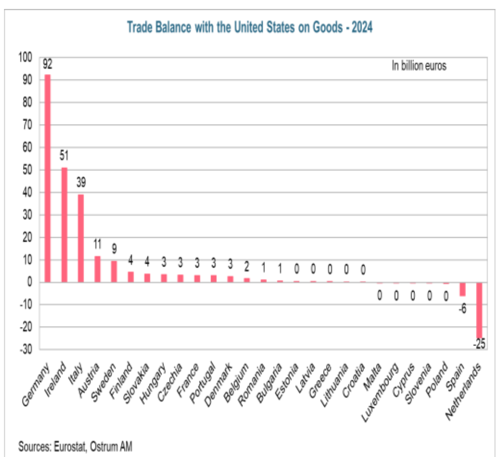


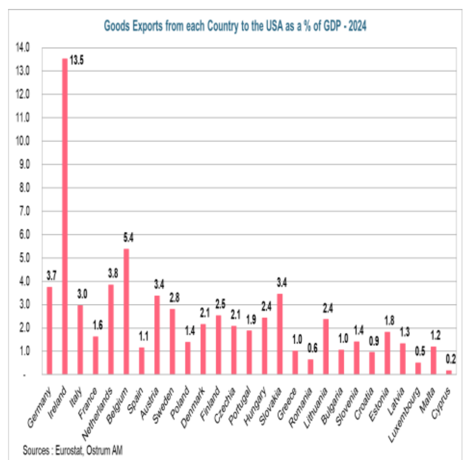
The EU has a trade surplus of nearly 200 billion euros with the U.S. in goods

The EU's trade surplus of 197.1 billion euros with the U.S. in goods in 2024 is primarily due to Germany (92 billion), Ireland (51 billion), and Italy (39 billion). In contrast, the Netherlands has a trade deficit of 25 billion euros in goods with the United States in 2024. The trade balance for other countries is nearly balanced, with France having a surplus of 3 billion euros.

Ireland is the most exposed to U.S. tariffs, followed by Belgium, the Netherlands, Germany, and Italy.

The share of exports to the United States as a percentage of GDP helps measure each country's exposure to U.S. tariffs. Ireland is by far the most exposed, as shown in the right graph. Irish goods exports to the U.S. represent 13.5% of Ireland's GDP, while this ratio is 5.4% for Belgium, 3.8% for the Netherlands, 3.7% for Germany, and 3% for Italy. France and Spain have limited exposure, with 1.6% and 1.1%, respectively.



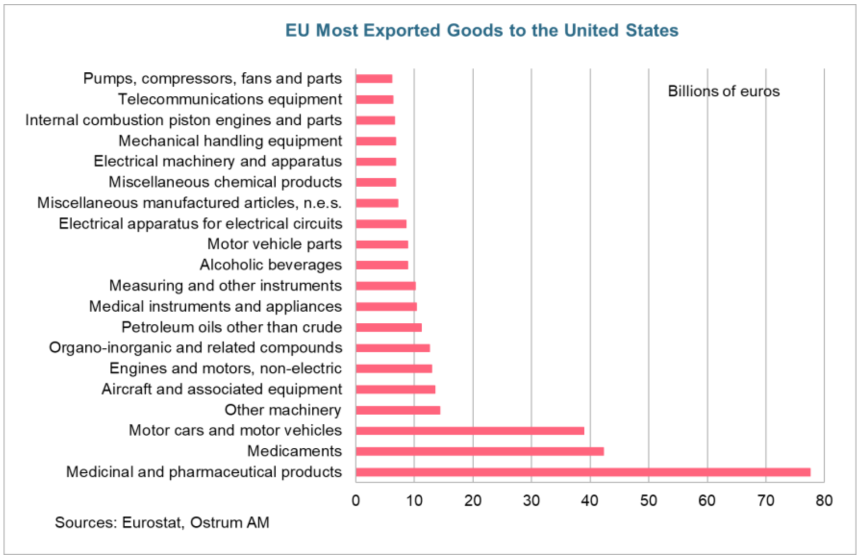


The EU primarily exports machinery and vehicles, as well as chemical products, to the U.S.

In terms of product groups, the EU primarily exports to the United States machinery and vehicles (38.8% of goods exports in 2024) and chemical products (32.2%). The most exported goods to the United States are, by far, medical products, pharmaceuticals, and medications, followed by cars.

The European goods most exported to the United States are by far medical products, pharmaceuticals, and medications, followed by cars.

Currently, pharmaceutical products are not subject to additional tariffs from the United States, but this could change. Ireland will be by far the most affected given the importance of the pharmaceutical sector in its economy. In February, Irish exports to the United States tripled compared to the previous year, with 91% of these exports being pharmaceutical products: chemicals and related products, including medical and pharmaceutical products. American business leaders have rushed to increase their inventories in anticipation of rising tariff barriers.



Retaliation by the European Union

The EU has suspended retaliatory measures against the United States regarding the 25% tariffs on steel and aluminum.

In response to the failure of negotiations regarding the 25% tariffs on steel and aluminum (imposed on March 12), the EU announced retaliatory measures against the United States (on April 9) targeting 22 billion euros worth of American products. These goods are selected in such a way as to affect Donald Trump's electorate: motorcycles, boats, household appliances, and certain agricultural products, including soybeans. These tariffs were set to be implemented in phases on April 15, May 15, and December 1. However, these measures have been suspended until July 14, following the 90-day suspension of U.S. reciprocal tariffs.

Negotiations between the EU and the United States have not yet begun

The EU primarily wants to negotiate, but the United States is not in a hurry and has not defined a clear position on its objectives.

The EU's goal is to negotiate with the Trump administration to avoid the implementation of these tariffs. During his last visit to Washington on April 14, European Commissioner for Trade Maros Sefcovic was unable to engage in serious discussions with his American counterpart. Negotiations have not yet begun, as the Trump administration has not defined a clear position on its objectives. Maros Sefcovic again proposed a duty-free agreement on industrial products, including cars, which had already been rejected, and left the door open to the removal of certain non-tariff barriers, without questioning sanitary and phytosanitary standards or digital regulations. The EU also reiterated that it was ready to purchase more American liquefied natural gas. One thing seems clear from the U.S. side: to maintain tariffs on steel, aluminum, and cars to encourage manufacturers to invest in the United States. During Giorgia Meloni's visit, Donald Trump expressed confidence in the possibility of an agreement with the EU, although he was not in a hurry to reach one.

In the event of a failure in negotiations, the EU could tax American services.

In the event of a failure in the negotiations and the potential implementation of 20% reciprocal U.S. tariffs on July 9, the EU is preparing retaliatory measures. These could target American services imported by the EU. Indeed, while the EU has a trade surplus with the United States in goods, it has a deficit in services trade of -109 billion euros in 2023.

In an interview with the Financial Times on April 10, Ursula von der Leyen clearly indicated that

The European Commission could tax advertising revenues from digital services and use the anti-coercion tool.

the EU was prepared to target American services imported by the EU, potentially including a tax on advertising revenues from digital services that would affect major tech companies like Amazon, Google, and Facebook. She also referenced a potential tax on scrap metal exports to the United States. The President of the European Commission stated that the EU could utilize the anti-coercion tool, which can impose restrictions on trade, investments, and financing. This instrument allows the EU to increase tariffs, restrict the trade of services and certain commercial aspects of intellectual property rights, limit access to foreign direct investments, and public procurement. It also enables the EU to demand that third countries remedy the harm caused.

In the event of a failure in negotiations and as a deterrent measure, the EU is considering imposing export restrictions. This could be done through the imposition of quotas, licenses, or even the prohibition of exporting certain critical goods to the United States that are difficult to substitute.

Trade diversion towards the EU

The very high tariffs between China and the United States will result in a strong decline in trade between the two countries and a diversion of trade towards third markets. The World Trade Organization estimates that Chinese goods exports are expected to increase by 4% to 9% in all regions outside North America, including a 6% increase in Europe, due to these changes.

The EU fears a massive influx of highly competitive Chinese products that can no longer be sold in the United States due to prohibitive American tariffs.

Ursula von der Leyen stated that she would not tolerate Chinese goods affected by U.S. tariffs being redirected to the EU. The EU has thus established a monitoring mechanism and indicated that it would take safeguard measures if an increase in Chinese imports is detected. This aims to protect the EU from a massive influx of highly competitive Chinese products. The EU already announced last October a potential tariff of up to 35% on imports of Chinese electric cars due to unfair competition linked to massive public subsidies. Negotiations are ongoing with China to replace these tariffs with minimum prices on Chinese electric car exports. The EU is also likely to face an influx of American products that can no longer be sold in China. In France, the chemical industry, represented by France Chimie, has raised the alarm. It estimates that 10 to 20 billion euros worth of Chinese products could flood the EU, along with 5 to 10 billion euros worth of American products, while the industry is already weakened.

Strengthening intra-zone trade

Barriers to intra-European trade remain significant. They are estimated to be equivalent to tariffs of 44% for goods trade and 110% for services trade, according to the IMF.

In the face of the trade war with the United States, the EU has intensified trade negotiations with other countries such as Malaysia, Thailand, the Philippines, Indonesia, and the United Arab Emirates. Beyond forming partnerships with other economies, it is essential for the EU to strengthen its intra-zone trade. According to the IMF, this trade is far from functioning within a true single market, which is supposed to ensure the free movement of goods, people, services, and capital within the EU. The IMF estimates that trade barriers are still significant, equivalent to average effective tariffs of 44% in goods trade (three times higher than trade among U.S. states) and 110% in services trade. In comparison, the average effective tariffs on trade outside the EU are 3%. Given that EU countries primarily trade among themselves, strengthening the single market could significantly boost growth and generate productivity gains. According to the IMF, reducing these barriers to the level of those in the United States would result in a 7 percentage point increase in productivity in the long term. To achieve this, the IMF recommends investing in cross-border infrastructure, liberalizing protected sectors, continuing significant liberalization of intra-zone trade, and harmonizing regulations among member states.

Conclusion

The trade war will heavily impact world trade and activity. Beyond the direct effect on EU exports, the consequences are expected to be more significant on household and business confidence. Investment, employment, and consumption will be affected. In this context, the ECB has lowered its rates for the seventh consecutive time and has left the door open for further cuts. The EU, for its part, must take measures to strengthen the single market and reduce the barriers to trade that remain too high.

Aline Goupil-Raguénès

Market review

Coming Up for Air

A welcome calm has settled over the markets, with bond and credit markets easing and equity volatility slightly diminishing, despite ongoing uncertainties surrounding the international geopolitical landscape and the impact of tariff measures.

As the markets enter a fragile peace ahead of the long Easter weekend, discussions have begun between Japan and the United States, while China outlines its conditions for dialogue—emphasizing respect and Taiwan—while attempting to rally the Asian bloc against U.S. trade policies. Europe is exploring targeted measures and is rekindling dialogue with the U.S. regarding the Ukrainian crisis. However, these signs of de-escalation do not completely obscure the operational and financial risks associated with customs duties. Chinese logistics are adapting, but overall cargo orders have plummeted. While current stockpiles provide a few weeks' visibility on production, shortages are expected to re-emerge swiftly. The Philadelphia Fed's manufacturing survey has sharply deteriorated in April, plunging to -26.4 from +12.5 in March. This decline in orders is compounded by rising costs. In China, first-quarter growth has proven stronger than expected, at +5.4% year-on-year. Household consumption stands at 5.9%, and industrial production accelerated by +7.7% in March, driven by export demand that has spurred activity. However, housing investment remains in contraction, down 10% compared to 2024, even as foreign direct investment in China shows improvement. The strengthening of consumption is timely as China seeks to rebalance its growth. The yuan's exchange rate has stabilized around 7.30 against the dollar.

On the financial markets, the yield on the 10-year U.S. Treasury note has fallen from 4.55% to approximately 4.32% at Thursday’s close. Jerome Powell has drawn the ire of Donald Trump by highlighting the risks posed by his tariff policy to economic activity and inflation. Price shocks are concerning consumers but are expected to be secondary to growth and employment. Moreover, financial stability is a prerequisite for achieving macroeconomic objectives. Consequently, the slope of the U.S. yield curve continues to steepen, with the 5-30 year spread widening by 15 bps over four sessions. Trading volumes are naturally subdued ahead of the Easter weekend. Recent Treasury auctions (20-year and 5-year TIPS) have been adequately absorbed by the market. Upcoming transactions for maturities of 2 to 7 years will serve as a new test of investor appetite for U.S. debt. The Bund remains a safe haven, with the European Central Bank's (ECB) rate cuts intensifying downward pressure, particularly as Christine Lagarde distances herself from the concept of interest rate neutrality. The ECB is leaving all options open in light of cyclical risks, with the Bund trading below 2.50%. Price action is also favorable for sovereign debt, with the OAT trading at a spread of 77 bps against the Bund, while the BTP has fallen below the 120 bps threshold. Inflation appears underestimated, with 2-year breakevens below 1.50%. Credit spreads are easing, particularly in synthetic indices benefiting from declining equity volatility. European equity markets are rebounding (+3/4%), despite a pullback in technology stocks (ASML, export restrictions on Nvidia). Oil stocks are regaining strength, and financials are resuming their upward trajectory.

Axel Botte

Main market indicators

G4 Government Bonds	22-Apr-25	1wk (bp)	1m (bp)	2025 (bp)
EUR Bunds 2y	1.64%	-13	-49	-44
EUR Bunds 10y	2.46%	-7	-30	+10
EUR Bunds 2s10s	82.1 bp	+6	+19	+54
USD Treasuries 2y	3.78%	-6	-17	-46
USD Treasuries 10y	4.42%	+9	+17	-15
USD Treasuries 2s10s	63.3 bp	+15	+34	+31
GBP Gilt 10y	4.6%	-5	-11	+3
JPY JGB 10y	1.32%	-6	-20	-2
€ Sovereign Spreads (10y)	**22-Apr-25**	**1wk (bp)**	**1m (bp)**	**2025 (bp)**
France	77 bp	+1	+6	-6
Italy	111 bp	-7	-2	-5
Spain	70 bp	-1	+7	+1
Inflation Break-evens (10y)	**22-Apr-25**	**1wk (bp)**	**1m (bp)**	**2025 (bp)**
EUR 10y Inflation Swap	1.86%	+2	-19	-7
USD 10y Inflation Swap	2.36%	+3	-11	-10
GBP 10y Inflation Swap	3.23%	+8	-19	-30
EUR Credit Indices	**22-Apr-25**	**1wk (bp)**	**1m (bp)**	**2025 (bp)**
EUR Corporate Credit OAS	112 bp	-8	+20	+10
EUR Agencies OAS	56 bp	-1	+7	-6
EUR Securitized - Covered OAS	53 bp	+1	+8	-4
EUR Pan-European High Yield OAS	396 bp	-28	+77	+78
EUR/USD CDS Indices 5y	**22-Apr-25**	**1wk (bp)**	**1m (bp)**	**2025 (bp)**
iTraxx IG	73 bp	+2	+15	+15
iTraxx Crossover	373 bp	+7	+67	+59
CDX IG	74 bp	+3	+17	+24
CDX High Yield	442 bp	+20	+105	+130
Emerging Markets	**22-Apr-25**	**1wk (bp)**	**1m (bp)**	**2025 (bp)**
JPM EMBI Global Div. Spread	367 bp	-7	+33	+41
Currencies	**22-Apr-25**	**1wk (%)**	**1m (%)**	**2025 (%)**
EUR/USD	$1.150	1.959	6.499	11.1
GBP/USD	$1.338	1.111	3.521	6.9
USD/JPY	JPY 140	2.038	7.374	12.0
Commodity Futures	**22-Apr-25**	**-1wk ($)**	**-1m ($)**	**2025 (%)**
Crude Brent	$67.1	$2.3	-$4.5	-8.7
Gold	$3 467.3	$236.6	$456.3	32.1
Equity Market Indices	**22-Apr-25**	**-1wk (%)**	**-1m (%)**	**2025 (%)**
S&P 500	5 158	-3.83	-8.99	-12.3
EuroStoxx 50	4 901	2.37	-9.64	0.1
CAC 40	7 230	1.76	-10.11	-2.0
Nikkei 225	34 221	-0.14	-9.17	-14.2
Shanghai Composite	3 300	0.98	-1.93	-1.6
VIX - Implied Volatility Index	32.47	5.11	68.41	87.1

Source: Bloomberg, Ostrum AM

Additional notes

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