

Client Update

Our views on US tariffs

April 2025

News about US reciprocal tariffs have rocked global markets, as President Trump announced sweeping import taxes that were far higher and affected a much broader swathe of countries than expected. Given how fluid the situation still is, we don't have particularly strong views at this point, but our broad take is that the tariffs are being used primarily as a negotiation tool – an attempt to drive more manufacturing back into the US. Whether that will actually work is another question.

If high tariffs do remain in place, it is clearly negative for the global economy – the inflationary impact alone would be significant, and the US would not be immune to that. In addition, there is an increased risk of counter-tariffs on US services (where the US runs a large surplus versus the rest of the world), which is why, structurally, we struggle to see them being sustained over the longer term. That said, if negotiations to reduce tariffs fail to appease the US, this could potentially trigger a global recession.

If we take the announcements from the White House at face value, our view is that within a global emerging markets context, Latam – and in particular, Mexico – looks relatively better positioned. The US-Mexico-Canada agreement has been honoured, reciprocal tariffs have been avoided, and Mexico stands to benefit from increased nearshoring. While a US recession would also weigh on Mexico, given the trade links, so far it looks like a net positive for the region.

As for China, we think it is also relatively well placed in this environment. Its direct gross exports to the US as a percentage of its Gross Domestic Product (GDP) have already declined, which means the impact will be less severe than in previous cycles. More importantly though, until now, the government has held back from deploying

aggressive domestic stimulus, likely in anticipation of escalating trade frictions. That means that there is scope to support consumption more meaningfully, which should benefit our domestic-focused holdings – companies like Huazhu Group, a multi-brand hotel group in China, China Resources Beer, the leading brewery in China, and Tencent, China's leading super-app and games company.

For Chinese exporters, the issue is that a lot of its production has already shifted to Vietnam, Bangladesh, and others – and now those countries are being hit even harder with tariffs. Indeed, the bigger fall-out from Trump's tariffs will be the countries that are focused on low-end manufacturing – especially where products lack pricing power and margins are already thin. The combination of weaker demand (due to higher prices) and limited ability to pass on costs will hit both volumes and profitability. That said, intra-regional exports among emerging markets – that is, emerging markets trading with each other – have been growing steadily and now makes up almost half of emerging markets' total exports,¹ which could mitigate the impact of US tariffs.

In India, which is mainly a domestically focused economy and doesn't have much US trade exposure (goods exports to the US account for just 2% of its GDP²), the main impact will likely be on its IT services industry. The likes of Tata Consultancy Services and Infosys don't face tariff risks as service providers, but growth will likely slow if a global recession ensues. On the other hand, we believe revenue is unlikely to decline sharply – these businesses are cost leaders and manage large portions of their clients' systems. Furthermore, strong cash flow and the nearly 100% pay out to shareholders provide some downside cushion.³

¹ Source: International Monetary Fund, Direction of Trade Statistics (DOTS); Emerging markets' exports to emerging markets accounted for 46% of emerging markets' total exports in the 12 months to the end of November 2024.

² Source: World Economics, Office of the United States Trade Representative, using 2024 figures.

³ Source: All company data herein retrieved from company annual reports or other such investor reports. As at 8th April or otherwise noted.

Well positioned to navigate the uncertainty

From a portfolio perspective, even in a more adverse scenario, we remain confident in our holdings' ability to navigate the environment, as they have done in the past. Our companies are characterised by strong competitive advantages – whether in brand strength, distribution, or cost leadership – and have historically managed to preserve margins and profitability across cycles, despite headwinds. Most of our portfolio holdings have strong balance sheets (net-cash) which should allow them to weather a difficult period and invest counter-cyclically to gain market share.

Moreover, most of our holdings are domestically focused businesses. We do own some exporters – but these are quality companies with strong competitive advantages and, in many cases, there are no good alternatives to their products and services. One key holding in this segment is TSMC, which effectively holds a natural monopoly in leading-edge nodes, and with that, pricing power. Its customers don't have an alternative to substitute for TSMC's advanced chips. There are near-term concerns about slowing AI-related investment by the large US technology companies, but the current valuation reflects some of these concerns already.

We also own Techtronic, a leading power tools company in the US with a large portfolio of products sold under the well-known Milwaukee and Ryobi brands. Techtronic has steadily gained market share in the US and other markets over the past 15 years through innovation and job-site support for its customers. Although its manufacturing footprint is much more diversified (beyond China) compared to Mr Trump's first term as president, it now faces high tariffs on Vietnam, where it manufactures about 40% of its products. Techtronic's peers face a similar situation and the whole industry may have to increase prices to pass on these costs. While not ideal, we believe that Techtronic is better placed as the market leader and with relatively higher gross margin. It is run by a strong management team who navigated the changes well last time. It has sold off materially on these concerns and is currently on around 15x 2024 earnings.⁴

Our holdings in India's domestically oriented sectors – the leading private banks like HDFC Bank and ICICI Bank and domestic consumer companies like Godrej Consumer and Colgate India, for example – should be less impacted.

On that front, we were in Mumbai on a research trip in February; and the sentiment was certainly less exuberant than it was six months ago, which we see as a positive sign. It suggests that expectations are becoming more grounded. Overall risk-reward still doesn't seem particularly attractive compared to other markets but we expect growth in India to be fine. From here, it will likely be more of a stock-pickers' market – similar to 2016-19.

Net-net, while the tariffs are clearly bad news for markets in general, at the headline level, we believe that our holdings are likely to remain resilient through this period. The majority of our portfolio holdings have more cash than debt on their balance sheet, and average return on equity remains healthy and well above the overall market. We were expecting earnings to grow at low to mid-teens over the next few years, though there is a possibility this could prove too optimistic, depending on how long the high tariffs stay in place. But given that valuations have already corrected we think our portfolios look attractive from both an absolute and relative perspective.

Outlook

The economic uncertainty has only increased following the actions of the newly elected government in the US. We don't pretend to know the end-result of the significant disruption to global trade nor are we trying to predict such outcomes. However, it is in times like this that the conservative approach with which we manage our portfolios comes to the fore.

Although the current disruption might have an impact over the near term, the majority of our holdings have net-cash balance sheets, which provides them with a significant opportunity to invest counter-cyclically or use mergers and acquisitions, as opportunities arise, to gain market share. Moreover, the owners and managers of our investee companies have experienced several such periods of disruption, most recently during the pandemic. They have established track records of navigating the uncertainty well.

Overall, we believe our holdings in market-leading businesses are likely to remain resilient through this period, and the long-term outlook for Asia and emerging markets, led by secular growth trends and underpinned by rising incomes, remains unchanged.

⁴ Source: Financial metrics and valuations are from Bloomberg and Factset. As at 8th April 2025 or otherwise noted.

Important Information

This material is for general information purposes only. It does not constitute investment or financial advice and does not take into account any specific investment objectives, financial situation or needs. This is not an offer to provide asset management services, is not a recommendation or an offer or solicitation to buy, hold or sell any security or to execute any agreement for portfolio management or investment advisory services and this material has not been prepared in connection with any such offer. Before making any investment decision you should conduct your own due diligence and consider your individual investment needs, objectives and financial situation and read the relevant offering documents for details including the risk factors disclosure. Any person who acts upon, or changes their investment position in reliance on, the information contained in these materials does so entirely at their own risk.

We have taken reasonable care to ensure that this material is accurate, current, and complete and fit for its intended purpose and audience as at the date of publication. No assurance is given or liability accepted regarding the accuracy, validity or completeness of this material.

To the extent this material contains any expression of opinion or forward-looking statements, such opinions and statements are based on assumptions, matters and sources believed to be true and reliable at the time of publication only. This material reflects the views of the individual writers only. Those views may change, may not prove to be valid and may not reflect the views of everyone at First Sentier Investors.

Past performance is not indicative of future performance. All investment involves risks and the value of investments and the income from them may go down as well as up and you may not get back your original investment. Actual outcomes or results may differ materially from those discussed. Readers must not place undue reliance on forward-looking statements as there is no certainty that conditions current at the time of publication will continue.

References to specific securities (if any) are included for the purpose of illustration only and should not be construed as a recommendation to buy or sell the same. Any securities referenced may or may not form part of the holdings of First Sentier Investors' portfolios at a certain point in time, and the holdings may change over time.

References to comparative benchmarks or indices (if any) are for illustrative and comparison purposes only, may not be available for direct investment, are unmanaged, assume reinvestment of income, and have limitations when used for comparison or other purposes because they may have volatility, credit, or other material characteristics (such as number and types of securities) that are different from the funds managed by First Sentier Investors.

Selling restrictions

Not all First Sentier Investors products are available in all jurisdictions.

This material is neither directed at nor intended to be accessed by persons resident in, or citizens of any country, or types or categories of individual where to allow such access would be unlawful or where it would require any registration, filing, application for any licence or approval or other steps to be taken by First Sentier Investors in order to comply with local laws or regulatory requirements in such country.

This material is intended for 'professional clients' (as defined by the UK Financial Conduct Authority, or under MiFID II), 'wholesale clients' (as defined under the Corporations Act 2001 (Cth) or Financial Markets Conduct Act 2013 (New Zealand) and 'professional' and 'institutional' investors as may be defined in the jurisdiction in which the material is received, including Hong Kong, Singapore, Japan, and the United States, and should not be relied upon by or be passed to other persons.

The First Sentier Investors funds referenced in these materials are not registered for sale in the United States and this document is not an offer for sale of funds to US persons (as such term is used in Regulation S promulgated under the 1933 Act). Fund-specific information has been provided to illustrate First Sentier Investors' expertise in the strategy. Differences between fund-specific constraints or fees and those of a similarly managed mandate would affect performance results.

About First Sentier Investors

References to 'we', 'us' or 'our' are references to First Sentier Investors, a global asset management business which is ultimately owned by Mitsubishi UFJ Financial Group (MUFG). Certain of our investment teams operate under the trading names AlbaCore Capital Group, FSSA Investment Managers, Stewart Investors and RQI Investors all of which are part of the First Sentier Investors group.

This material may not be copied or reproduced in whole or in part, and in any form or by any means circulated without the prior written consent of First Sentier Investors.

We communicate and conduct business through different legal entities in different locations. This material is communicated in:

- **Australia and New Zealand** by First Sentier Investors (Australia) IM Ltd, authorised and regulated in Australia by the Australian Securities and Investments Commission (AFSL 289017; ABN 89 114 194311)
- **European Economic Area** by First Sentier Investors (Ireland) Limited, authorised and regulated in Ireland by the Central Bank of Ireland (CBI reg no. C182306; reg office 70 Sir John Rogerson's Quay, Dublin 2, Ireland; reg company no. 629188)
- **Hong Kong** by First Sentier Investors (Hong Kong) Limited and has not been reviewed by the Securities & Futures Commission in Hong Kong. First Sentier Investors, FSSA Investment Managers, Stewart Investors, RQI Investors and Igneo Infrastructure Partners are the business names of First Sentier Investors (Hong Kong) Limited.
- **Singapore** by First Sentier Investors (Singapore) (reg company no. 196900420D) and this advertisement or material has not been reviewed by the Monetary Authority of Singapore. First Sentier Investors (registration number 53236800B), FSSA Investment Managers (registration number 53314080C), Stewart Investors (registration number 53310114W), RQI Investors (registration number 53472532E) and Igneo Infrastructure Partners (registration number 53447928J) are the business divisions of First Sentier Investors (Singapore).
- **United Kingdom** by First Sentier Investors (UK) Funds Limited, authorised and regulated by the Financial Conduct Authority (reg. no. 2294743; reg office Finsbury Circus House, 15 Finsbury Circus, London EC2M 7EB)
- **United States** by First Sentier Investors (US) LLC, authorised and regulated by the Securities Exchange Commission (RIA 801-93167)
- **Other jurisdictions**, where this document may lawfully be issued, by First Sentier Investors International IM Limited, authorised and regulated in the UK by the Financial Conduct Authority (FCA ref no. 122512; Registered office: 23 St. Andrew Square, Edinburgh, EH2 1BB; Company no. SC079063).

To the extent permitted by law, MUFG and its subsidiaries are not liable for any loss or damage as a result of reliance on any statement or information contained in this document. Neither MUFG nor any of its subsidiaries guarantee the performance of any investment products referred to in this document or the repayment of capital. Any investments referred to are not deposits or other liabilities of MUFG or its subsidiaries, and are subject to investment risk, including loss of income and capital invested.

© First Sentier Investors Group