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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 GDP[2]), 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