Tariff Turbulence

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Trump Threatened New Tariffs on Canada, Mexico, and China

Over the weekend, President Trump unveiled a new set of tariffs targeting goods imported from Canada, Mexico, and China. The new policy included a 25% tariff on goods coming from Canada and Mexico, with the exception of Canadian fuel imports, which faced a reduced 10% levy. Additionally, Trump announced goods imported from China would incur a 10% tariff. The tariffs were set to be made effective after 12:01 a.m. on Tuesday, before Mexican President Claudia Sheinbaum and Canadian Prime Minister Justin Trudeau were able to strike a deal with President Trump to delay the start date by 30 days after productive talks between the governments on Monday. However, there was no reprieve for China following a conversation between Trump and Chinese President Xi Jinping. The 10% levy on Chinese goods went into effect overnight, and China delivered a calculated response with a 10% tariff of its own on approximately 80 U.S. products (including energy products) taking effect on February 10, plus a probe into Alphabet's Google (GOOG/L) regarding breaches of anti-trust laws and tighter export controls on critical minerals. This overall move to implement tariffs marks a clear shift in U.S. trade policy, as the new administration now aims to more directly address trade imbalances and strengthen domestic industries by imposing higher duties on these key trading partners.

A Bull Market in Near-Term Uncertainty

The current situation remains fluid, and looking ahead, investors should be prepared for the possibility of additional tariff announcements. President Trump recently signaled that the administration may also implement tariffs on specific categories of goods, such as semiconductors, pharmaceuticals, and steel. He has also suggested the potential for tariffs on European imports. Additionally, the administration has said it could escalate tariffs in response to any retaliatory actions from its trading partners. There is also speculation that these tariff announcements may all just be part of a broader strategy to negotiate key diplomatic objectives and will only prove to be short-lived.

Another layer of uncertainty arises from how businesses and consumers will react to tariff hikes if they become longer-lasting. Many anticipate that businesses would pass the full cost of the tariffs on to consumers. However, if businesses expect additional tariffs in the future, they might raise prices by more than the tariff cost. On the other hand, some consumers, particularly those with lower incomes, have already shown resistance to higher prices, which could force businesses to absorb part of the tariff burden. It is a lot to work through, and this intricate combination of dynamic factors will likely create some macroeconomic volatility in the short term as the true duration, scope, and ultimate impact of these new policies remains unclear.

U.S. Stocks Preferred Amid Global Tariff Uncertainty

Global equity markets traded lower in reaction to the announcements on Monday, as markets had generally been pricing in some relief from tariff risks after the inauguration. The general response over the last year has been for non-U.S. equities to underperform U.S. equities on tariff fears, and that appears to remain a risk going forward.

fixed income, the bear flattening of the yield curve seen on Monday indicates the bond market views tariffs as a short-term inflation risk and a potential problem for growth further out.

The LPL Research Strategic and Tactical Asset Allocation Committee (STAAC) currently prefers U.S. stocks over developed international and emerging markets (EM) on a geographic basis. The domestic preference stems primarily from superior earnings and economic growth in the U.S., which is reinforced by the policy stances of the new administration and a stronger U.S. dollar, which is usually supported by tariffs.

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This research material has been prepared by LPL Financial LLC.

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Kristian Kerr drives the broad, house investment strategy for LPL Financial Research. His career includes over 25 years of industry experience.