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Wealth Advisory Market Update

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Market and Economic Implications of Recent U.S. Tariff Announcements

The announcement of retaliatory tariffs earlier this month has elicited a pronounced response from financial markets and key sectors of the economy. The newly imposed tariffs target 185 countries with a baseline rate of 10%. However, significantly higher rates have been applied to countries with which the United States maintains large trade deficits. Japan, Vietnam, and the European Union now face tariff rates of 24%, 46%, and 20%, respectively. Notably, China is subject to a staggering 245% tariff on its exports to the U.S. Unlike traditional reciprocal trade measures, this policy framework is explicitly centered on correcting trade imbalances—marking a substantial shift in the U.S. approach to international trade.

On April 9th, the administration announced a 90-day pause on tariff enforcement for all countries except China, as negotiations commenced. This announcement sparked a relief rally, with the S&P 500 posting its third-largest single-day gain since World War II. Market sentiment and economic forecasts have since become highly reactive to trade-related news. For instance, Goldman Sachs had recently identified a recession as its base-case scenario. However, following the pause announcement, the firm rescinded that outlook and no longer forecasts a near-term recession. At present, many analysts remain in a holding pattern, awaiting further clarity on the direction and potential outcomes of the ongoing negotiations.

Despite concerns reflected in soft economic indicators, hard data has yet to confirm a significant downturn. Federal Reserve Chairman Jerome Powell has repeatedly cited this divergence as justification for maintaining the current interest rate policy. While consumer spending has moderated, employment data—including hiring and layoff metrics—remains stable, underscoring the labor market's resilience. Inflation data, particularly in the services sector (which constitutes over 70% of the overall inflation reading), has also come in below expectations in recent reports.

Conversely, warning signs are emerging in credit markets. High-yield credit spreads experienced their sharpest two-day widening since the onset of the COVID-19 pandemic, and credit default swaps have seen a notable surge. In addition, rising delinquencies in auto loans and credit card debt—reaching levels not seen since 2011—have raised further concerns about consumer financial health.

The bond market, particularly the long end of the yield curve, has experienced significant volatility. The 30-year Treasury yield saw its largest weekly increase since 1987, while the 10-year yield experienced its biggest weekly rise since 2001. Under normal circumstances, market stress drives investors toward the safety of Treasuries, pushing yields lower. However, current conditions reflect a lack of liquidity, with bid-ask spreads widening to levels not seen since the pandemic. There is growing speculation that China may be offloading U.S. Treasuries in favor of the yuan as a retaliatory measure.

Compounding this instability is the prevalence of the “basis trade” among hedge funds. This arbitrage strategy involves buying or selling Treasury bonds while simultaneously shorting or buying the corresponding futures contracts. The strategy is highly leveraged—sometimes up to 20 times—which amplifies risk. As yields rise, margin calls are forcing funds to unwind positions, driving yields even higher. A similar situation in 2019 prompted Federal

Reserve intervention. Current estimates suggest the scale of the trade is even larger today. Treasury Secretary, Scott Bessent, has acknowledged the situation and has indicated a willingness to intervene, if necessary, though he does not currently see the need for action.

In the absence of a resolution to the tariff negotiations and greater policy clarity, heightened market volatility is likely to persist. The economy, which has been buoyed in recent years by substantial fiscal stimulus—averaging $1 trillion every 90 days—has thus far avoided a recession. However, consumer debt burdens are rising, and personal savings rates remain historically low, indicating that consumers may be reaching their financial limits. The imposition of these tariffs may serve as a catalytic shock, revealing underlying vulnerabilities and potentially precipitating an economic slowdown.

There remains considerable uncertainty surrounding both the economy and financial markets as the new administration begins to implement its policy agenda. We are committed to navigating these challenging times with diligence and care, and we remain available to address any questions or concerns you may have. Thank you for your continued trust—we look forward to more stable and prosperous times ahead.

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