HSBC Mutual Fund

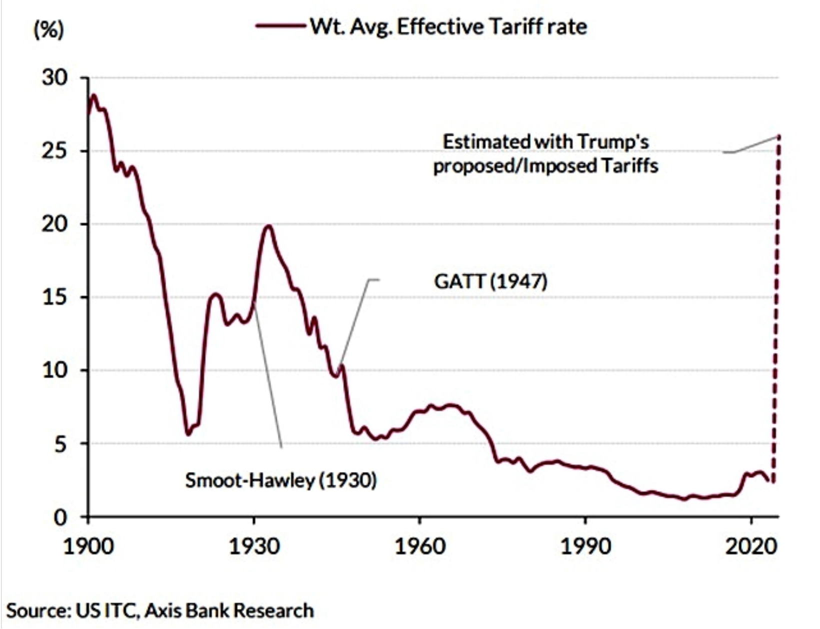
Tariff Impact

Markets in a state of flux

In a much-watched out event globally, USA on ‘Liberation Day’ (April 2) announced tariffs across most countries which will have financial, economic and political implications world-over. In the below note, we highlight the key implications of this event and our positioning in light of these events.

What has happened?

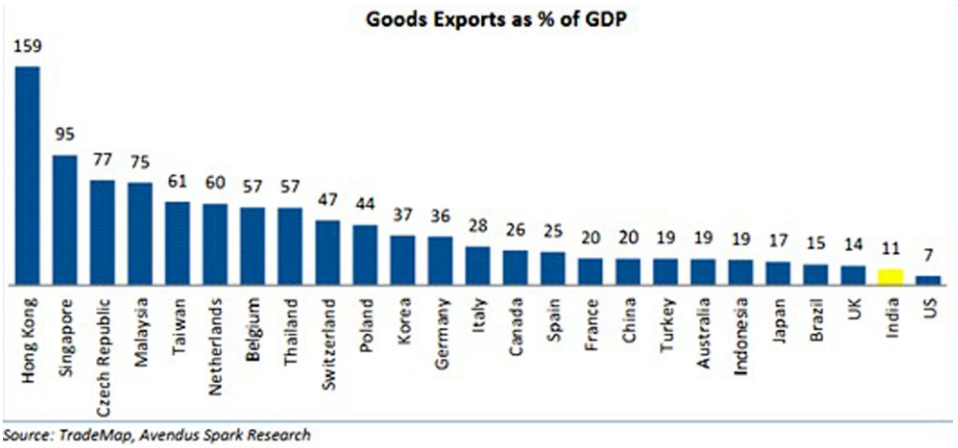
- US has announced 10% baseline tariff on all countries, effective from April 5, and reciprocal tariffs on 180 countries, effective from April 9, for ‘unfair’ trade practices.
- The quantum of reciprocal tariffs announced are much higher than that expected by the market.
- On an average, this results in weighted average tariff for the US increasing to 24%, from just 2.5% at the beginning of the year.



- There are certain goods which are not subject to reciprocal tariffs such as (I) steel, aluminum articles and auto/ auto parts which were already subject to Section 232 (Trade Act of 1962) tariffs earlier this year (ii) copper, pharmaceuticals, semiconductors and lumber articles (iii) bullion (iv) energy and certain minerals not available in US and (v) all articles that may be subject to Section 232 tariffs in future.

India's export exposure to US

- The contribution of India's merchandise exports to GDP is 11% ($430bn) and among the lowest in Emerging markets, limiting the impact of global trade slowdown.



- Among the top 5 export categories to US, Electronics (incl machinery) is the highest with 22% share of US exports, followed by gems and jewellery (14%), pharmaceutical products (11%), textiles (10%) and energy (9%).

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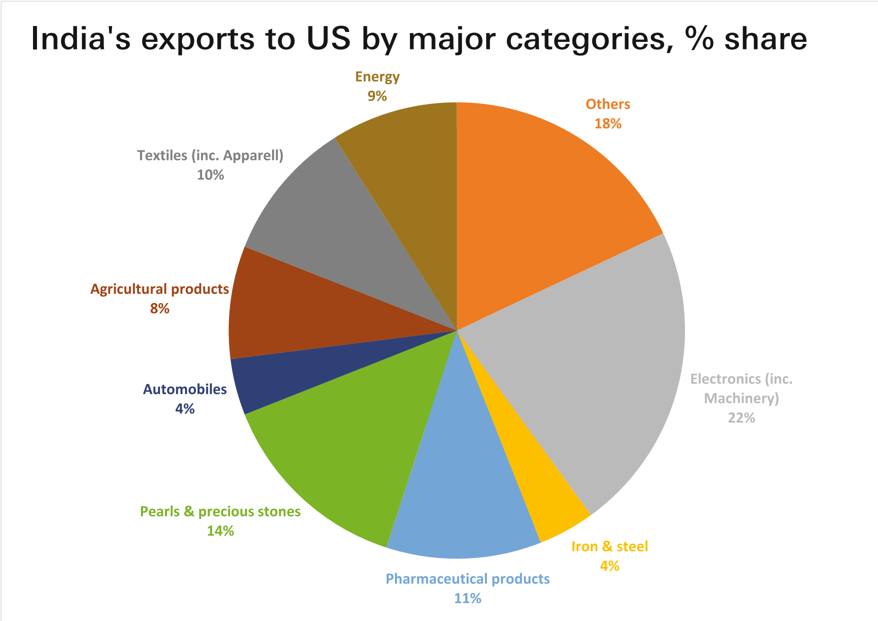
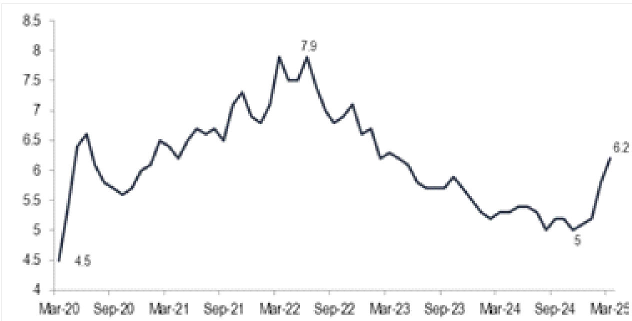


Source: UN Comtrade. UBS

Equity market implications

- The above steps, if implemented in current form, will lead to higher inflation in US, and could decelerate the US GDP growth rate (see chart below).

US Consumer Inflation expectations

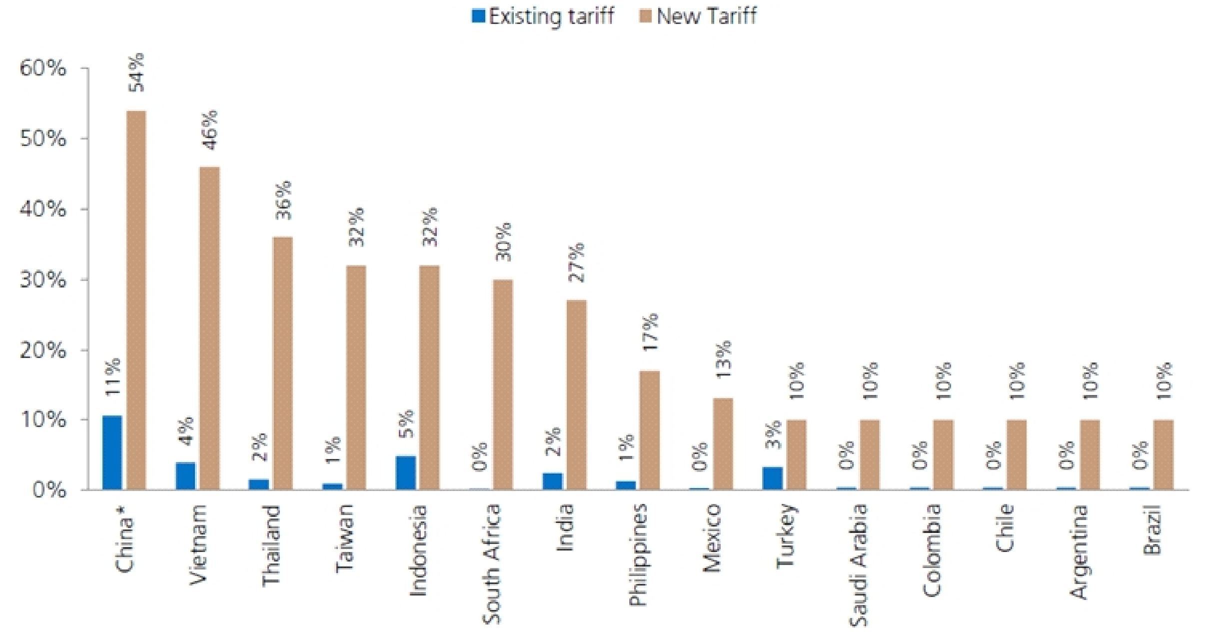


Source: Bloomberg, Investec Equities research

US CEO confidence in the economy 1Y from now

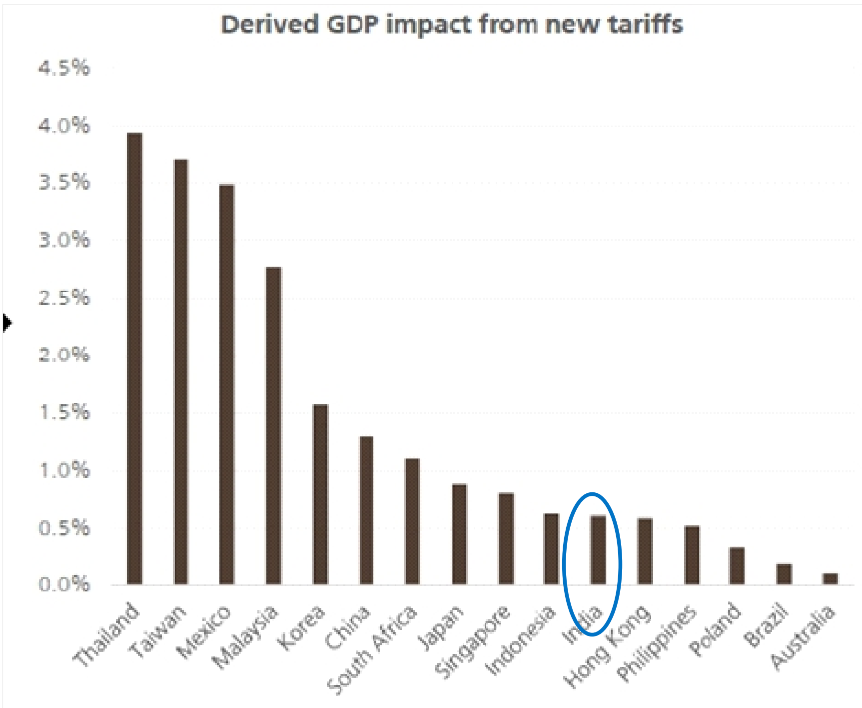
Source: Bloomberg, Investec Equities research

- We believe that the current tariff announcements are just a start, and the final outcome may take months to materialize based on how individual countries deal with these tariffs.
- Some countries, like India, are already in negotiations with US counterparts to cut tariffs on some US imports and working out a bilateral trade negotiation. Some others, like China and EU, are talking about retaliatory tariffs to protect their own interests.
- Notwithstanding the ongoing trade talks with US counterparts, **India relatively stands better placed vs most Asian peers.** The tariff imposed on India was 26% vs China 34% (over and above 20% tariffs already imposed), Vietnam 46%, Sri Lanka 44%, Bangladesh 37%, Thailand 36%, Indonesia 32%, Taiwan 32%, South Korea 25% and Japan 24%



Source: The White House, UBS. Note: *While it is not fully clear, the new tariffs are likely 'additive' to existing tariffs.This report looks at the impact from the additional tariffs announced 3rd April US Eastern Time.

- India's export to US as a percentage of GDP is low at 2.1% which should result in **lower GDP impact (50-60bps impact) when compared to Asian peers** (see chart below).



Source: The White House, CEIC, UBS

- On domestic front, high frequency macro indicators are improving with government . capex announcements, easing liquidity situation, rate cuts and expected bumper Rabi harvest.
- To conclude, while India seems relatively better placed, we think the **global uncertainty will result in Indian equity markets being volatile over the coming months.** Any sizeable market correction on these concerns should offer a great opportunity for wealth creation for investors with medium to long-term horizon.

Portfolio positioning and sectoral impact

- With some signs of slowdown in macros in 4QCY24, over the past 3-4 months, we had already started **reducing our exposure to mid and small caps** across all our funds with increase in large caps.
- At sector level, we had also **reduced our exposure to Capital Goods and Technology companies.** On the other hand, we had increased exposure to Banks and NBFCs.
- Post the tariff announcements, these are still early days, and we are talking to companies/ experts and monitoring the developments. However, based on the current announcement of tariffs we have attempted to look at some sector impacts:
  - **IT:** US/ global growth slowdown may lead to guidance cut across companies.
  - **Metals:** Potential global growth slowdown is likely to impact commodity demand and prices.
  - **Oil & Gas:** Lower crude oil prices are negative for upstream companies but benefits downstream/ oil marketing companies.
  - **Auto and auto ancillaries:** One large OEM will face challenges as US accounts for 33% of their European subsidiary revenues. There is likely to be a direct impact on some of the auto ancillary companies who are supplying to US and indirect repercussions through its supply chain to EU OEMs exporting to the US.
  - **Textile:** Large export to US for some of the companies. Tariff on India is lower than competitor (China, Bangladesh and Vietnam) which may be beneficial for some textile companies.
  - **Pharma:** No tariff announced for now, but indications are these are likely to be imposed. Generics should be relatively less impacted.

- **Chemicals:** Some companies have 20-25% export to US. India is at an advantage relative to China as tariffs + duty on Chinese crop protection are 54% to 79% vis à vis 27% to 32% for India. Brazil, with a 10% tariff, could see new crop protection capacities. Similarly, UAE, with a 10% tariff, could see new refrigeration gas capacities.
- **EMS:** Only one EMS player has 40-50% of sales is to US. Opportunity of export for other players due to differential tariffs with China.
- **Industrials:** MNC firms that already have manufacturing facilities in US and are importing from their Indian subsidiaries could consider expanding their US facilities. Cable companies have low single digit exposure to US, so likely to have marginal impact.

Note: Data as on April 7, 2025 or latest available.