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Chief Investment Office GWM
Investment Research

Tariffs begin to impact US inflation

UBS House View - Daily US

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From the studio

Podcast: **Ahead of the curve with Ulrike Hoffmann-Burchardi** (7 min)
Video: **CIO mid-year checklist – Portfolio steps with Jon Gordon** (6 min)

Thought of the day

US economic data have so far shown limited impact from President Donald Trump's trade policies. The latest labor data suggest that US companies have yet to start laying off workers, and investor sentiment has remained resilient, with the S&P 500 near its all-time high.

But inflation is beginning to show signs of picking up. The consumer price index (CPI) rose 0.3% in June, up from 0.1% in May, pushing the annual inflation rate to 2.7%—its highest level since February. Core inflation, which excludes food and energy, increased 0.2% on the month, up from 0.1% in the prior month, bringing the annual rate to 2.9%. While these figures were in line with expectations, they highlight the gradual impact of tariffs on prices. Apparel and household furnishings, which are tariff-sensitive categories, saw price increases, while vehicle prices declined.

Markets will now turn their focus to economic data in the coming days, including the producer price index, retail sales, industrial production, and the University of Michigan consumer sentiment survey. These reports will help investors gauge the health of the US economy and assess the Federal Reserve's next move.

Our base case remains for the US central bank to resume policy easing in September, bringing interest rates 100 basis points lower over the next 12 months.

Trump's tariffs should only be a modest boost to inflation. While the June inflation data showed mixed evidence of tariff-related price pressures, we believe the US effective tariff rate will settle at around 15%, lifting inflation only modestly. Tariffs are gradually impacting retail prices—a trend we expect to persist through 2026, and any upward surprises in inflation could complicate the Fed's ability to justify rate cuts. However, core services inflation, despite flattening recently, should start trending lower again, helping to prevent overall inflation from rising sharply—even if some tariffs are increased further on 1 August. Notably, shelter inflation, which accounts for over 35% of the CPI and has been the biggest single driver of overall

What to watch: 17 July 2025

- US retail sales, import and export prices for June
- US NAHB housing market index
- Japan June trade balance
- Various Fed speakers
- Second quarter results from TSMC, Netflix, Novartis, and others

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inflation, is expected to continue slowing. This, coupled with a weaker labor market, should allow the central bank to cut rates later this year.

The labor market has shown signs of weakening. While the US economy added more jobs than expected last month, the details of the labor report were weaker than the headline numbers. Private sector payrolls increased at the slowest pace since October last year, while average hourly earnings rose at the lower end of the post-pandemic range. The labor participation rate also fell to its lowest level since December 2022. These data points suggest that labor demand is deteriorating, as businesses are cautious about long-term hiring plans amid trade and economic headwinds.

Fed comments suggest rate cuts are on track this year. We do not expect a rate cut at the Fed's policy meeting later this month. However, the fact that some officials favored a reduction as soon as July suggests that policymakers are alert to softening economic activity and falling consumer confidence. We continue to expect the Fed to react according to available data, while speeches by a number of Fed officials later this week may give markets additional insights into the US central bank's path toward further easing.

So, we think the appeal of cash will be further eroded as rates fall later this year. Investors should lock in more durable sources of income, including through high grade and investment grade bonds. Long-term investors can also consider diversified fixed income strategies.

Caught our attention

US tariff watch: 19% for Indonesia. President Donald Trump on Tuesday said the US has reached a preliminary trade deal with Indonesia that will include a 19% tariff on Indonesian goods exported to the US. US exports to Indonesia will face zero tariffs, and Indonesia will commit to major US purchases, with Trump mentioning USD 15bn in energy products, USD 4.5bn in agricultural goods, and 50 US-made Boeing jets. Goods from third party nations shipped through Indonesia would face a higher (not yet disclosed) tariff, in a move echoing the Vietnam deal seen as targeting Chinese transshipment. Trump had previously threatened Indonesia with a 32% tariff on "Liberation Day" in April and in his trade letter sent last week. Speaking with reporters, Trump suggested talks with India were developing "along that same line." Talks with the European Union appear more challenging, with the EU Commission reportedly preparing to target EUR 72bn in US goods for retaliation if tariff talks fail.

Our view: Pending more details, the US-Indonesia trade deal appears better than expected for Indonesia. The direct tariff impact is modest since US exports represent just 1.3% of Indonesia's GDP (after exemptions), which is among the lowest in Asia. There are also no major US exporters present in the MSCI Indonesia benchmark index. Within the market, we continue to favor banks with competitive funding, high dividend yielding stocks, and select secular consumer businesses. India appears next in line for a similar agreement, though a benign outcome is at least partially priced, with earnings growth the main driver of our Attractive view on the market. More broadly, we continue to expect additional trade developments to emerge before the new 1 August deadline and for the US effective tariff rate to settle

at around 15%. Such a backdrop would allow risk assets to move higher over the next 12 months amid a resilient economy.

Investor enthusiasm for tech reaches 16-year high. Tech stocks have led the rebound in equities following the sell-off caused by US President Trump's "Liberation Day" tariffs in April. Between April and July of this year, allocations to the tech sector saw their largest three-month increase since March 2009, according to a Bank of America survey. The tech-heavy Nasdaq has climbed more than 35% from its April lows, setting a fresh record on Tuesday, while NVIDIA became the first chipmaker to reach a USD 4 trillion valuation. This resurgence reflects growing optimism that the "Magnificent 7" tech giants will continue delivering robust earnings growth, despite lingering concerns over tariffs and regulatory risks. Second-quarter earnings from Microsoft, Meta, Alphabet, Amazon, Apple, and Tesla in the coming weeks will provide further clarity on demand trends and sector fundamentals.

Our view: The recent rally in large-cap tech and AI stocks has been driven primarily by price-to-earnings (P/E) multiple expansion, as investors focus on future growth rather than current earnings performance. Without taking any single-name views, we remain structurally bullish on AI and the broader tech sector, but we also believe sustainable gains should be supported by upward revisions to earnings per share (EPS) rather than valuation expansion alone. Continued improvement in profitability and operational performance will be critical for maintaining momentum, particularly as valuations remain elevated. With second-quarter results approaching, we expect earnings surprises to play a key role in shaping sentiment, but caution that investors should remain mindful of stretched valuations and focus on long-term fundamentals. We recommend investors seek diversified exposure across semiconductors, software, and internet platforms, rather than concentrating risk in any single segment or individual stock.

Market update

Percent change. For volatility indices, net change in points. For valuation, change in price to earnings per share. For yields, net change in bps

16.07.2025	Current (*)	1D	5D	1M	YTD
VIX Index	17.4	+0	+1	-2	+0
MOVE Index	89	-2	+5	-5	-10
S&P 500	6244	-0.4%	+0.3%	+3.5%	+6.2%
S&P 500 trailing P/E (**)	24.7x		-0.1x	+0.8x	+0.1x
S&P 500 forward P/E (**)	22.3x		+0.0x	+0.7x	+0.8x
S&P 500 forward P/E ex-Mag 7 (**)	20.2x		-0.1x	+0.5x	+1.3x
Russell 2000	2205	-2.0%	-1.1%	+3.8%	-1.1%
Euro Stoxx 600	544	-0.2%	-1.1%	-0.5%	+7.2%
Shanghai Composite	3504	-0.0%	+0.3%	+3.4%	+4.5%
US 10-year Treasury	4.48	+0	+15	+4	-9
US 2-year Treasury	3.95	+1	+11	-2	-29
Germany's 10-year Bund	2.71	+0	+4	+19	+35
Germany's 2-year Bund	1.88	-0	+3	+4	-20
EURUSD	1.162	+0.2%	-0.8%	+0.5%	+12.2%
EURCHF	0.93	-0.2%	+0.1%	-0.9%	+0.3%
USDCHF	0.80	-0.0%	+0.9%	-1.5%	-11.7%
USDJPY	149	+0.0%	+1.8%	+2.9%	-5.3%
Brent crude, USD/bbl	69	-0.2%	-2.3%	-6.3%	-8.1%
Gold, USD/oz	3347	+0.3%	+0.8%	-1.5%	+26.7%

(*) or last close if not available, (**) weekly update

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