CIO Perspectives

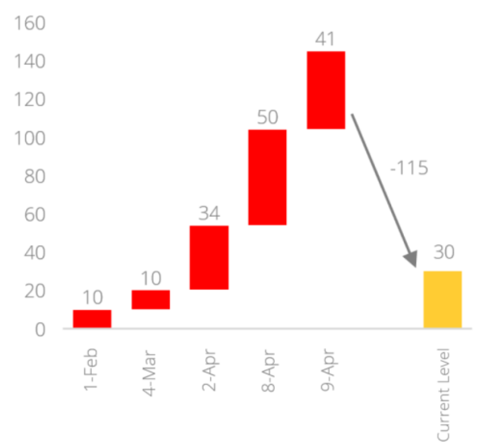
14 May 2025

DBS Chief Investment Office

Key Points

- US-China trade war de-escalated sharply with respective tariffs lowered by 115 %pts for next 90 days
- The speed at which this truce is concluded suggests that economic impact from the tariff war is starting to bite for both sides
- Best-case scenario after 90 days will be for the crisis to de-escalate further on the back of a "purchase agreement" from China and a potential fentanyl deal
- But prevalence of policy uncertainties will still compel China to diversify its exports from the US while doubling down on domestic consumption
- The V-shaped market recovery from the "Liberation Day" tariff sell-down underlines the importance of staying invested
- Equities: Stay positive on Tech amid robust investments on AI and strong opportunities for semiconductor and the technology supply chain
- Bonds: Stay overweight on high quality credit in 2-3Y bucket as a cash alternative; steeper yield curve provides opportunity to pick up good quality credit in 7-10Y bucket
- Gold: Continue to advocate for gold as a risk diversifier in investors' portfolio amid heightened recession risk

Figure 1: Additional US tariffs on China (%)



Source: Bloomberg, DBS

ASSET ALLOCATION

Portfolio Resilience in Era of Policy Ambiguity

Rapid tariff de-escalation: Possible reasons. The US-China trade war de-escalated sharply following the meetings in Geneva, with both countries agreeing to reduce tariffs on each other by 115 %pts for the next 90 days. Unsurprisingly, both parties presented their decision as stemming from a position of power, each claiming victory. Who blinked first? While pundits will debate on who blinked first, the answer invariably lies somewhere in between.

What we do know is that the US had overplayed its hand by ratcheting up tariffs (prompting tit-for-tat retaliation from China), and the economic impact is starting to bite for both sides, as evidenced by the speed at which the truce has come to pass.

Make no mistake. A tariff of 145% essentially represents a trade embargo for US/China at a time when US President Trump is experiencing waning poll numbers at home. More tellingly, recent moves to adopt policies of the progressive left, such as tax increases for top earners and pharma price cuts, underline Trump's urgency in boosting his popularity before the 2026 midterms and, above all, reframe the Republican party as one for the working class. Juxtaposed against this backdrop, it should not come as a surprise that Trump is keen to taper trade tension with China to avoid the economic repercussions of a full-blown trade war.

The road ahead: Possible scenarios. What might happen after 90 days? Using the first Trump presidency as a guide, a best-case scenario will be further de-escalation, with China agreeing to significantly reduce trade deficits with the US. A deal to curb exports of fentanyl from China will be another positive if US and China manage to reach an agreement. However, one should be mindful that even with a best-case scenario, things are no longer the same. The prevalence of policy uncertainty will compel China to diversify where it exports to, while doubling down on domestic consumption. While these changes take time, the trade volume between US and China will nonetheless be eroded.

Lessons from "Liberation Day" tariff sell-down: Stay invested. If the "Liberation Day" tariff sell-down has taught us anything, it will be for investors to stay invested. The recent correction serves as a great reminder of the challenges inherent with trying to "time the markets". Indeed, attempting to predict the highs and lows of markets is a fool's errand. Based on a study by JP Morgan, a fully invested position in S&P 500 over the last 20 years would have resulted in annualised returns of 10.2%. Miss the 10 best trading days and that drops to 6.0% (nearly a 40% haircut). The study also notes that seven of the 10 best days occur within 15 days of the 10 worst days. This tight clustering suggests that if fear pushes an investor to exit during times of market volatility, there is a high chance they will also miss out on the subsequent snapback rallies. To navigate the upcoming periods of policy ambiguity, listed below are our cross-asset recommendations:

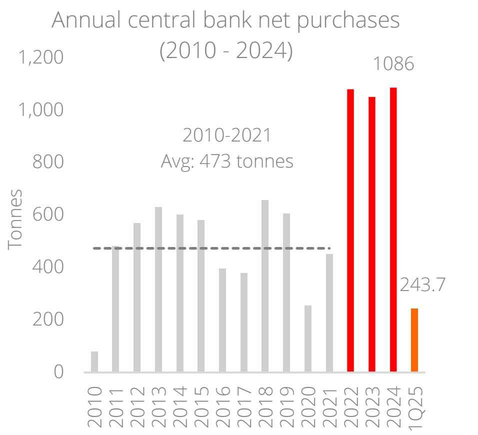
Equities:

- The latest US-China trade deal is not a silver bullet by any means, but any thawing of relations is a welcome change of pace for investors, especially in the tech sector. The tech-heavy NASDAQ composite surged more than 4.3% on Monday following this positive development. While investors continue to digest the news and consider further implications, there remains plenty of reasons to be positive on the technology.
- Investment in AI continues to be robust; Microsoft, Amazon, and Google plan to invest a combined USD250bn in 2025 on AI infrastructure, data centres, chip procurement, and next-gen algorithms to drive ecosystem growth. Similarly, the Middle East is stepping up its efforts to ensure not being left behind in the AI revolution, with an estimated USD100bn in AI-driven technology investments over the remainder of the decade.

Figure 2: Spreads have tightened from post-Liberation Day heights

Source: Bloomberg, DBS

Figure 3: Structural tailwinds at play – Central bank gold buying remains robust



Source: Bloomberg, DBS

- The commitment of global capital from West to East highlights the strategic importance of AI infrastructure and reinforces the long runway of opportunities for the semiconductor and technology supply chains worldwide. Against this backdrop, we continue to favour technology as a core pillar on the growth side of our barbell strategy.

<u>Bonds</u>:

- With trade risks abating, we expect credit spreads to remain sanguine as they have been over the last two years, based on (a) a general strengthening of corporate balance sheets as corporates have been preparing for trade uncertainty, and (b) a trend of net credit upgrades signifying improving fundamentals. IG spreads have tightened from their YTD high of c.120 bps to 98 bps at present.
- Stay overweight on high quality credit in the 2-3Y bucket as a cash alternative, while the steeper yield curve provides once again another opportunity to pick up good quality credit in the 7-10Y bucket in a credit duration barbell construct.

<u>Gold</u>:

- Notwithstanding the latest developments in the US-China trade war, we continue to advocate for gold as a risk diversifier in investors' portfolios. The 90-day deadline on the tariff pause means that while recession risk may have temporarily abated, it is still on the cards. Furthermore, as long as Trump remains in office, it is reasonable to assume that US policy risk and uncertainty will remain elevated.
- Recession risk aside, there are additional tailwinds for gold at play, including elevated central bank and investor demand on the back of geopolitical uncertainty and fragmentation, as well as monetary debasement risk from the growing US fiscal deficit. Such tailwinds are structural in nature and will not alter significantly with the passing of a single trade deal. Against this backdrop, gold remains one of the most optimal risk diversifiers for investors as it hedges against multiple key risks.

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