Trump's tariffs spark a closer look at Europe

Sandra Haurant considers how Trump's tariffs may have shifted investor attitudes towards the European equities market

Summary
- Prior to the US tariff announcements, a shift in portfolios away from the US and towards the European equity markets was already becoming visible.
- The trade tariffs, and the resulting uncertainty around their impact, has pushed many towards the relative stability of traditionally 'defensive' European markets.
- Some argue Europe offers diversification through its many and varied territories and sectors, with the potential for growth.
- Spending boosts on infrastructure and defence expected from the new German Chancellor (who is encouraging similar strategies from EU counterparts) makes the country look appealing.
- The detail, and subsequent impact, of the US import taxes are still uncertain and careful decisions on next steps are essential.

Former British Prime Minister Harold Wilson is credited with coining the phrase "a week is a long time in politics". It feels like something of an understatement today. Although it was only 2 April, Donald Trump's announcements of a raft of tariffs on global trade already feels like a long time ago. As a quick recap, a base tax of "up to 10 per cent" on imported goods was announced, with 20 per cent tariffs for imports to the US from the European Union.

While this was double the 10 per cent taxes imposed on UK-origin imports, the EU's rate was much lower than tariffs placed on Chinese imports, which quickly rose to 30 per cent, then 104 per cent, then 145 per cent, as the two superpowers squared up to one another. At the time of writing, tariffs were paused at 10 per cent almost across the board, with the notable exception of China, which still faced an 145 per cent import tax on goods.

Atlantic crossing?

Quite how policies such as the tariffs will impact European equity markets depends on multiple, complex factors. But even prior to the US announcements, concerns around the new administration's policies had been contributing to a shift in investor attitudes.

Russell Investments head of multi asset EMEA, Alain Zeitouni, says: "For years, the US has been considered the premier destination for investors, buoyed by the tech boom and dominance of mega-cap stocks. US assets have also been the default safe haven in times of global uncertainty, with investors focusing on the dollar and US treasuries."

And, he adds: "At the end of 2024, foreign investors owned around 18 per cent of the US equity market, compared to less than 5 per cent in 2000, and, of those 18 per cent of foreign investors, 50 per cent are European. So, it is a fact that European investors have been allocating more and more of their capital to the US over the past 25 years."

But what if the former safe haven becomes the eye of the storm? Zeitouni argues: "If investor confidence in US treasuries as a reliable hedge diminishes, they may seek safer alternatives elsewhere. Given the relative appeal of European equities – stronger dividend yields, attractive valuations, and greater sectoral resilience – institutional investors should consider increasing their exposure to Europe."

Indeed, a shift has already begun to occur, Zeitouni says. "Looking at the ETF market, which tends to be an early indicator of global trends, we have seen a rotation out of US assets towards European assets since the first news on US tariffs announcement. Of course, it's too early to draw long-term conclusions from just two months of data, but there are early signs of a rebalancing between US and European assets."

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What's behind the European appeal?

According to Zeitouni, European equities "tend to offer more stable returns compared to many other global regions". Much of this is down to a heavier weighting in traditionally defensive sectors, like consumer staples, healthcare and utilities. "For example, when comparing sector weightings in the MSCI Europe index versus the MSCI USA, Defensive stocks represent 29 per cent of the index versus 19 per cent respectively," he says.

While these sectors might appear lacklustre in bull markets, this lower sensitivity to economic cycles can be a boon for pension schemes, "where security and stability are prioritised over high but volatile returns", says Zeitouni.

And then there is income. "European

equities have historically maintained a stronger dividend profile than other regions," says Zeitouni. "As of the end of Q1 2025, the dividend yields for the MSCI Europe and MSCI World indices stood at 3.1 per cent and 1.8 per cent, respectively. This is especially appealing for pension funds that value steady income streams to match regular outflows."

Room to grow

While the world is figuring out how the apparent new order will work, Vontobel portfolio manager, Markus Hansen, argues that Europe is, generally, looking positive. Faced with the US tariffs, he says: "European markets have performed better. This is likely due to relative better view of growth within Europe, which is seeing faster cuts in central banks rates. The ECB is now at 2.25 per cent and expected still to cut further."

Another reason, Hansen says, is increased fiscal spending plans, notably those laid out by Germany's new chancellor, Friedrich Merz, who took up office in May 2025, and who is encouraging similar spending in other EU countries. "EU markets were and remain 'cheap,' relatively, and benefit from the 'improving' relative growth momentum," Hansen says. "So, for us it makes sense to add more international and European companies to a global portfolio, compared to recent years of overweight US markets."

A story of sectors

Crucially, says Hansen, European equity markets can provide precious diversification potential. "In uncertain times, diversification helps to offset volatility, and European companies and markets offer some top global companies with quality growth predictable returns at compelling valuations," says Hansen.

And Europe is, of course, inherently diverse, replete with neighbouring but differing countries and varied sector specialisations, arguably making the

European equity market far greater than the sum of its parts.

L&G global equity strategist, Robert Griffiths, says: "The different countries across Europe offer a range of distinctive sector exposures, allowing investors to pick and choose countries depending on their view of the world, from the defensive of Switzerland to the financial-heavy Italian market."

Griffiths adds: "From here, we would highlight the UK equity market as a cheap form of protection against stagflationary concerns. Its mix of defensive and commodity sectors tends to perform well in times of rising stagflationary risk, something that any escalation of tariff concerns could contribute to.

"Beyond that, there remains significant engagement with German equities, where the prospect of infrastructure and defence spending continues to underpin investor enthusiasm, though we'd note the reliance of the German equity market on just a handful of names to drive performance over the last year or so."

And while certain industrial sectors will inevitably be more affected by US import taxes than others, the wider impact of these tariffs is likely to be far from uniform.

"Some of the most directly tariff-exposed sectors, most notably in areas like autos, beverages and pharmaceuticals, have been steadily underperforming the market, a trend which began last year," Griffiths says.

"What changed this year was a recognition of the extent to which tariffs would adversely impact major US companies and the broader US economy: While only the sales of European companies to the US would face additional duties, US companies face the prospect of both retaliation on all their international sales, and higher input costs. That has helped European indices to outperform even as equity markets globally sold off. In other words, tariff risks have created relative losers within the European equity market, but for the European equity market as a whole, it has come through this period of stress as a relative winner."

Next steps for European equities

It's never easy to predict the future, and it's virtually impossible when the political landscape is changing as often as British weather in summertime. Some things can be said with near certainty, though: The tariff talks will be complex, and the impact of both taxes and the ensuing uncertainty could well be long lasting.

"As such, the markets and more specifically the stocks that navigate this uncertainty not only remain important to own, but often emerge stronger once the uncertainty passes," says Hansen. "So, the focus on investment in quality growth companies should continue to see interest and to deliver the predictable and sustainable returns with lower volatility that we look for."

As for the duration of market wobbles, Hansen says: "The timeline for completing all the trade deals will be the first test of how long uncertainty may last."

Written by Jon Yarker, a freelance journalist