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Global trade redefined: Banking and capital markets

Dealing with tariff uncertainty

April 2025

This report has been developed in collaboration with the Strategy& team, PwC's global strategy house. Together, we transform organisations by developing actionable strategies that deliver results.

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Introduction

The imposition of US tariffs, while not directly targeting the UK banking sector - given their primary focus on goods rather than services - nonetheless has the potential to significantly impact UK financial institutions. The largest potential impact be the result of the broader impact on the economy in which UK Financial Institutions and their clients operate.

Global trade tensions and the resulting uncertainty have contributed to market volatility, which will have a knock-on effect on key revenue-generating activities for banks.

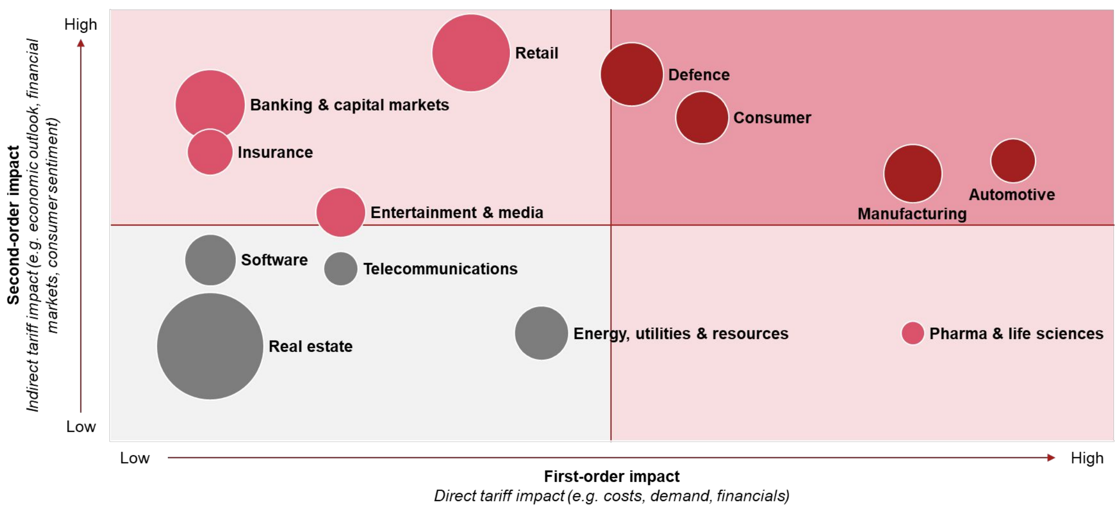
Investment banking functions such as IPOs, M&A, and both debt and equity capital markets are likely to experience dampened activity due to reduced corporate confidence and slower economic growth, particularly in export-dependent economies. On the flip side, market volatility will increase trading volumes, driving some revenue increase for the banks.

The market disruption has also heightened the strategic importance of scenario planning regarding the impact on liquidity and collateral management, especially for banks with global capital markets exposure, although they are generally more capitalised and better positioned to face shocks given the various regulatory reforms implemented since the 2008 global financial crisis.

Some common industry actions:

1. Assess first-order impact versus second-order impact
2. Understand variation by sector within an industry and interdependencies across industries
3. Adopt a mix of 'no regret moves' in the short term and strategic choices in the longer term
4. Identify both risk mitigants and growth opportunities
5. Embed ongoing resilience to respond to geoeconomic shocks

Illustrative US tariff exposure for UK business, by sector[1,2]



Notes: 1. Estimated tariff impact assumes measures stay in place for a prolonged period, in line with Strategy&'s 'Break and reorder' scenario; 2. Featured sectors account for c.60% of UK GVA (Gross Value Added); 3. Estimated 2024 GVA based on ONS data

Where we are today

On 2 April 2025, the US administration announced a sweeping package of tariffs on imported goods. It marked the country's most significant departure from liberal trade policy since the Smoot-Hawley Act of 1930. The scale of the measures suggests a structural pivot in US trade strategy. Given their breadth, and the growing likelihood of retaliatory responses from key trading partners, businesses now face a materially more volatile and uncertain global trading environment.

What happened on 'Liberation Day'?

The Executive Order introduced a dual framework of restrictions: broad-based 'baseline' tariffs alongside more targeted 'reciprocal' measures. The EU was subject to 'reciprocal' tariffs of 20%, China 34%, with certain South-East Asian economies facing higher rates still. The UK was included under the 10% 'baseline' category. Certain exemptions were made for pharmaceuticals, critical minerals and semiconductors.

Prior to this, there were also a number of product-level distinctions, for example steel and aluminium and automobiles were previously singled out with a 25% tariff.

On 9 April, reciprocal tariffs were paused for 90 days for most trading partners. The 10% 'baseline' tariff introduced on 5 April now applies for all countries, except China, for which a 145% tariff applies to most goods.

A further revision was introduced excluding smartphones, computers and other electronics. US officials have indicated that further sector-specific measures are likely. The international response has been mixed:

- **Retaliatory tariffs** from countries such as China and Canada, which have imposed tariffs on a wide range of US goods.
- **Diplomatic engagement** from the UK and EU, signalling efforts to secure exemptions or negotiate new terms.
- **Unilateral liberalisation** from a small number of economies, which have opted to remove tariffs on US imports entirely, albeit from a starting point where most US goods were not subject to tariffs.

Looking ahead

Recent US statements suggest further restrictions may be introduced in select product categories. Economic theory holds that when trade flows are disrupted, capital flows are rarely far behind.

Asset markets are already reacting. We've seen volatility across equities, fixed income and foreign exchange – some of which may reflect repositioning by non-US central banks, many of whom hold large exposures to US government debt. This adds another layer of complexity for firms already contending with uncertainty around tariffs, supply chains and pricing.

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Trade is the hinge between economic theory and political reality. When it swings, the whole house can shake."

Barret Kupelian, Strategy& and PwC UK Chief Economist

What could happen next

Three scenarios to plan for the short term

In the near term, scenario planning will be essential. Over time, a reassessment of supply chain configuration, investment strategy and risk management frameworks may prove unavoidable in the face of an increasingly fragmented global trading system.

To help clients better understand how tariffs could evolve, we've devised three scenarios. Given the unpredictable and fast changes happening, we've chosen to limit these to tariff policy. However, we are mindful that the current changes to US tariff policy is likely to spill over into second- and third-order impacts.

Stabilise and rebuild

Reversal of the US's position on tariffs, coupled with time-bound trade negotiations with its main trading partners, including Canada, Mexico and China.

To limit market uncertainty, there is regular forward guidance on the state of the trade negotiations. The US's main trading partners strike limited trade arrangements by the end of the 90 days suspension period (i.e. 8 July 2025). These come into force by the end of the calendar year. In the interim, the "baseline" tariffs continue to apply for most economies, including China.

Divide and deal

Reversal of US position on tariffs coupled with time-bound trade negotiations with some of the US's trading partners (EU, UK, Canada and Mexico included) but excluding China (and potentially some other South-East Asian economies).

- For those counterparts where a trade arrangement is agreed by 8 July 2025, these are put in place by the end of 2025/Q1 2026. In the interim, the "baseline" tariffs remain in place.
- For those counterparts where a trade arrangement is not agreed upon within the 90 days, reciprocal tariffs are re-imposed, consistent with the 2 April 2025 announcement.
- For China, tariffs remain in place consistent with the US's latest announcements and Chinese policymakers react in kind.

In the medium to long run, the ex-US G7 economies set up cooperation mechanisms which lead to gradually closer trading, regulatory and investment cooperation.

Break and reorder

Trade negotiations with most of the US's trade counterparts, including the EU, UK, Canada, Mexico and other advanced economies break down. The US doubles down on its necessity to swiftly eradicate the goods trade deficit with the rest of the world. The US reimposes "reciprocal" tariffs by 8 July 2025. With this in mind, the EU, Japan, China and other economies retaliate in equal measure. As these economies import less than they export to the US, retaliatory actions spill over into the services sector (e.g. digital services) and potentially to public procurement.

In the short to medium run, a subset of ex US G20 economies set up trade, regulatory and investment cooperation mechanisms at very rapid pace. In this scenario, we could also see some non-European economies seeking a Customs Union arrangement with the European Union. We could also see some South-East Asian economies forging closer trading relations with China. These changes are also rapidly reflected in investment flows.

Taking stock of tariffs

Understanding the impact on the banking sector

Tariffs are reshaping global trade flows and have the potential to expose UK banks to elevated credit risk, in those sectors most exposed to tariffs and complex supply chains. Additionally, inflationary pressure and interest rate uncertainty is creating economic uncertainty, including the potential for liquidity pressures, and will require banks to ensure the range and frequency of scenario planning is appropriate.

Yet amid the disruption, new opportunities are emerging. Banks are increasingly relied on for risk advisory, hedging solutions and strategic support, as clients adapt to shifting economic conditions.

The impact varies across the UK banking landscape, depending on individual banks' sector and geographical exposure. Institutions with a heavier footprint in Asia or the US may face more pronounced headwinds, while those focused on Europe or domestic markets may experience more muted effects. The table below outlines the key challenges and opportunities facing banks over the short, medium and long term in this evolving trade environment.

Horizon	Challenges	Opportunities
Shorter Term impacts **Longer term impacts**	• Potential deterioration in asset quality • Potential for risk in private markets to impact on wholesale markets • Credit demand drops amid client caution • Margin compression from falling rates • Deal flow slows amid uncertainty • Client draw-down on committed credit lines • Impact of tariffs on supplier and own cost base • Funding conditions tighten • Flight-to-safety flows result in reduced returns • Potential global interest rate divergence impacts global institutions • GDP slowdown drives credit rating downgrades and default risk with impact on capital requirements • Strategic uncertainty from geopolitical shifts • Regulatory fragmentation and erosion of global standard setting • Inability to realise global scale with fragmentation and divergence hindering common ops, tech and data	• Market volatility driving increased trading revenue • Increase in demand for treasury solutions and risk advisory • Increased demand for FX and hedging services • Interest rate reductions drive increased lending demand • Increased demand for advisory services and working capital optimisation e.g. to aid restructuring of supply chains • Opportunities created by shifting and new trade corridors e.g. trade finance • Strategic reallocation of capital for well capitalised and funded players via M&A or portfolio shifts • Booking centres and legal entity models are adapted to optimise regulatory and cost differentials

Navigating the potential fallout

Short and longer term actions you should take

In light of ongoing trade disruptions and tariff shifts, banks must adopt both short-term mitigation tactics and long-term strategic positioning to remain resilient.

Short-term ‘no regret’ moves	Moves to capture maximum value over the longer term
• **Credit risk reassessment:** Evaluate sector-level exposure - particularly to export-heavy clients and international supply chains - through rigorous stress testing and scenario modelling.	• **Portfolio diversification and rebalancing:** Review and manage exposure to tariff-exposed industries and the regions that are reliant on those sectors
• **Liquidity and capital planning:** Manage liquidity buffers and collateral with heightened awareness of global market volatility and US Treasury disruptions. Review funding strategies in anticipation of central bank policy shifts.	• **Trade finance opportunity:** Leverage capabilities in structured trade finance and hedging to support clients adjusting supply chains and trade corridors.
• **Scenario planning:** Implement robust planning around tariff timelines, FX fluctuations and customer behavior, especially considering potential new UK trade deals and the evolving UK regulatory stance.	• **Platform optimisation and digital acceleration:** Reconfigure capital structures and booking models for efficiency. Embrace digitisation and AI-driven risk operations to counteract margin compression.
• **Regulatory engagement:** Maintain clear lines of communication with regulators and policymakers. Align risk frameworks and lending behavior with national and international macroeconomic responses.	• **Strategic transformation and M&A:** Consider selective M&A and portfolio shifts to build scale, enhance competitiveness and prepare for potential divergence in global regulatory regimes.

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Whilst the banking sector is not directly, at this point at least, impacted by the recent tariff turmoil and is also significantly better capitalised and more resilient as a result of myriad developments since the financial crisis there will still be significant impacts both in the UK and Globally. Banking is of course tightly correlated to the real economy and the current disruption will create both challenges and opportunities over the coming period.”

Mark Batten, PwC UK Banking & Capital Markets Sector Leader

Key contacts

Contact us to discuss how best to respond to the changing rulebook for global trade.

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