Predictably unpredictable:
President Donald Trump and US exceptionalism in US markets

FOR FINANCIAL ADVISERS AND THEIR RETAIL CLIENTS

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Predictably unpredictable

Trump is back and as polarising and unpredictable as his last term in office. With the early stages of his presidency steeped in turbulence the question we are frequently asked is: what do you think he will do with tariffs? The next question is generally about the rest of his strategy.

The answer is that we don't know as we cannot read his mind. Some people think he will do well, that he is a Master of Game Theory and others think he is 'mad' and without a strategy.

We are not political strategists, nor game theorists: we invest portfolios and manage risk. With that in mind we find that diving into the fluid and ever-changing details is counterproductive, so it is better to look at the bigger picture.

Trump's mandate and the big picture

When Donald Trump was elected back in November, it was a foregone conclusion that he had a "mandate". He won not just the electoral college vote (which determines who becomes the president of the United States) but also the popular vote. He ran a populist campaign and vowed to make America great again, again! He was clear about the plans he had for the country and the direction in which he intended to travel. Issues like immigration, drugs, trade and manufacturing and the war in Ukraine were key aspects of his election campaign. Investors liked the strong positioning, and markets greeted the election result with a strong push upward in US markets, sentiment was strong.

Sentiment

Sentiment can be fickle and what we observed following the election result was a strong increase in consumer sentiment and confidence. US markets benefitted and the US Dollar soared. Whether this was an accurate reflection of the US economy remains to be seen. Trump has been in office just under 2 months.

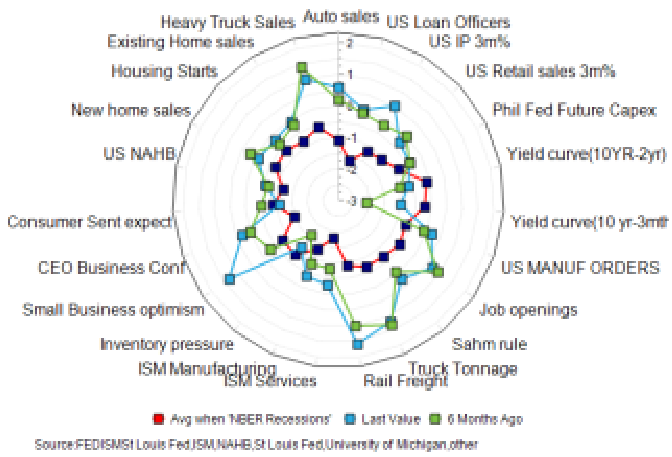
Similarly, the negative sentiment surrounding US stocks and the economy may not be an accurate representation of reality. So, while the approximate 16% shift upward in stocks was exceptional, the recent fall of about 14% is probably not a fair reflection of the health of the economy. Policy may change the direction of the economy both in the US and globally, and the data will lead our decision making.

Chart 1 - US Markets Over Six Months

Source: FE Analytics, March 2025

US recession watch

Chart 2 - US Recession Watch



Source: Zenith Investment Partners, March 2025

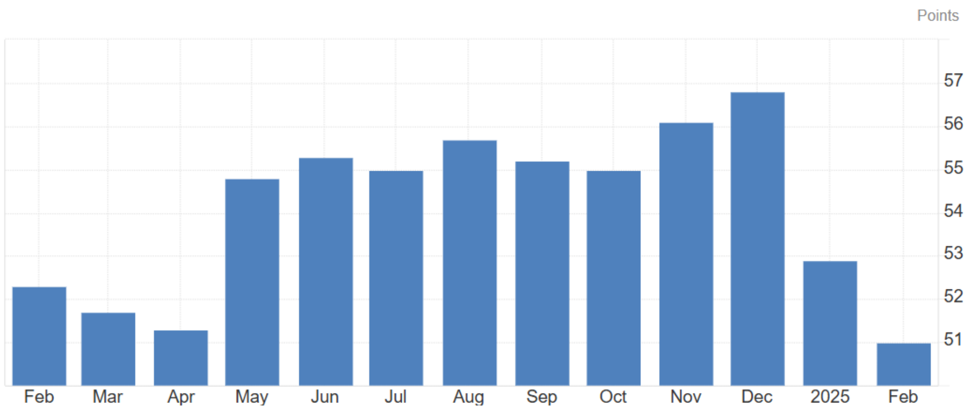
Current market sentiment is focussed on the risk of a recession. Data visualisation software from our sister company, Zenith Investment Partners, affords us insight into the current state of the US economy. When the US economy expands, data points in light blue below expand outward. When the economy slows the data points contract inward. The deep blue and red lines indicate average historical recessions. We would conclude that the US economy seems to be stable, with areas slowing down.

We cannot rule out some of the recent events have detracted from or contributed to the US economy, and for that we have forward-looking data that indicates the general direction of travel. It is too early to tell what affect the new administration will have on the economy, but we will be closely monitoring the data as it is released; early information indicates a slowdown but for now the US still sits on firm footing.

Forward looking data: US PMI and the economy

For the first time in two years, the US purchasing managers index for the services sector – a forward looking survey for economic activity by businesses - has contracted. Consumer sentiment is weakening, and business activity is contracting. Last week the manufacturing ISM for businesses showed a drop in new orders. Businesses also expect price increases in the future. Reading the comments by the survey respondents show that tariffs is their biggest concern.

Chart 3 - US purchasing managers index for both services and manufacturing



Source: Trading Economics, March 2025

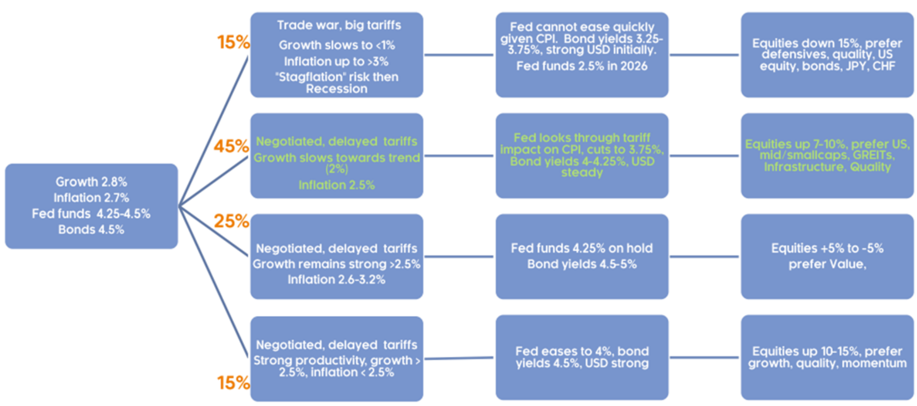
Tariff detail

When the President started making his tariff announcements, and at the time of writing, he initially proposed a 25% tariff on most goods from Canada and Mexico and 10% all goods from China. He also proposed 10% tariffs on Canadian oil. He then proposed a 25% tariff on steel and aluminium exporters, 25% on car and semiconductor chips, 25% on all goods from the European Union and reciprocal tariffs on countries who intended to pay back the US in kind. While this sounds straightforward, it's the changing timelines that are causing a lot of nervousness with businesses and investors alike. The risk with tariffs is that inflation edges higher or is stubbornly persistent.

The big picture: the management of uncertainty

Historically we have viewed the world through the lens of growth, inflation, and interest rates. You might visualise the cause-and-effect set of possible outcomes below. Tariffs have the potential to affect inflation and growth to varying degrees depending on the way in which they are implemented.

Focus: Plausible US scenarios to Jan 2026



Source: Zenith Investment Partners, March 2025

Our view of the world has not seen a significant change. We still think that inflation will moderate, and growth will slow below its elevated trend. There are risks and the risk of a recession, both mild and deep scenarios are 'non-zero' but are lower probability events. Tariffs might slow growth more than we expected but as we have seen, the US economy is doing well.

Chart 5 - Scenario Analysis

Nine Month Scenarios		FE Probability %	Zenith Probability %
Inflation remains high (PCE+3%)	Growth remains above trend	15.0%	15.0%
	Growth slows below trend	10.0%	0.0%
	Mild recession	0.0%	0.0%
Moderate inflation (PCE: 2-3%)	Growth remains above trend	15.0%	5.0%
	Growth slows below trend	**40.0%**	**60.0%**
	Mild recession	5.0%	5.0%
Inflation drops (PCE<2%)	Growth remains above trend	2.5%	0.0%
	Growth slows below trend	5.0%	0.0%
	Mild recession	5.0%	10.0%
	Deeper Recession (Something breaks)	2.5%	5.0%

Source: Zenith Investment Partners, March 2025

Outlook for markets

Sentiment has changed suddenly over the 6 months – from investors being overly optimistic to somewhat pessimistic. Donald Trump has adopted a punchy strategy for implementing his policies, 'move quick and don't be afraid to break things' would be an apt description of his philosophy. It has resulted in market uncertainty which is compounded by the intricacies of various aspects of policy he is working on at the same time.

The big picture points to a slowdown in the US – and likely other economies around the world – however the data on the US economy is not as bad as sentiment would indicate. This may well change, and we will continue to monitor the data and adapt the portfolios to the environment.