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Investment Insights Monthly

From the Desk of Bill Hornbarger, Chief Investment Officer February 2025

There's a New Tariff in Town

Following through on one of the major talking points of his campaign, President Trump has imposed tariffs on a variety of goods, with promises of more to come. In one of his latest moves, he signed a proclamation to "close existing loopholes and exemptions to restore a true 25% tariff on steel and elevate the tariff to 25% on aluminum." The details surrounding the when and what of tariffs have been fluid. At one point, the White House announced 25% across-the-board tariffs on Canada and Mexico beginning on February 1, only to later indicate that specific items (pharmaceuticals, steel, aluminum and microchips) would be subject to tariffs. Other members of the administration have suggested a gradual approach, starting at 2.5% on all goods and then slowly increasing tariffs. He has also announced a 10% tariff on imports from China. More recently, President Trump has moved to impose reciprocal tariffs "almost immediately" on a wide variety of countries. Reciprocal tariffs are straightforward in theory: The U.S. would pose the same levies on imported goods from a given country that the other country imposes on its U.S. imports.

The bottom line is that the Trump Administration views tariffs as a key component of policy. The bigger question is how it views the goals of tariffs. Are they viewed solely as a means to raise revenue, or as a tool to bring other countries to the negotiating table to bring trade and trade policies more into balance? President Trump and his advisors have often referred to the "tariff sheriff," former President William McKinley, who as a representative supported the Tariff Act of 1890, which came at a time of great prosperity for the United States. It raised the average duty on imports by almost 50% to protect domestic manufacturers and ultimately resulted in steep price increases for consumers.

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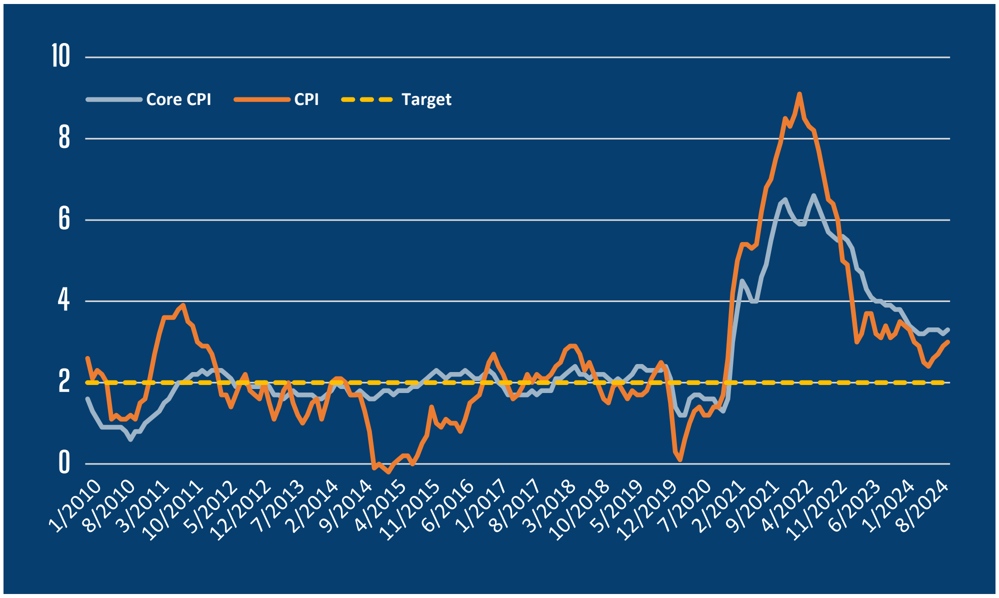
We believe the biggest reason for tariffs currently is a negotiating tool to bring other countries to the table to recalibrate trade policies. Tariffs can change consumers' behavior and dissuade them from buying goods from other countries, hurting the economies of those nations, leading many to seek agreements to reduce or avoid tariffs. Howard Lutnick, President Trump's choice to be Secretary of Commerce, specifically delineated between the plan to impose duties on Mexico and Canada as an emergency measure to achieve border security and longer-term plans for tariffs. He indicated that the threatened 25% tariff is not a "tariff per se" but a way to force the two countries to further secure the borders. In a post on Truth Social, President Trump wrote that the recent move to impose reciprocal tariffs was for "purposes of fairness" and "For purposes of this United States Policy, we will consider Countries that use the VAT [value-added tax] System, which is far more punitive than a Tariff, to be similar to that of a Tariff. Sending merchandise, product, or anything by any other name through another Country, for purposes of unfairly harming America, will not be accepted."

In terms of the economic impact, history suggests that tariffs are growth-negative in terms of gross domestic product for the countries involved, and that both consumers and companies would be negatively impacted both from a growth and inflation perspective. And it's not just the added costs of tariffs that are potentially inflationary, supply chains could be negatively impacted and experience loss of both profitably and pricing power.

Speaking of Prices

The Consumer Price Index (CPI) for January jumped more than expected, accelerating from 0.4% month-over-month (MoM) to 0.5%, well above the expected 0.3%. Core inflation followed suit, up 0.4% versus 0.3% expected. That put the year-over-year (YoY) increases at 3.0% and 3.3%, respectively, moving further away from the U.S. Federal Reserve's (Fed's) 2% target. Services in general and shelter specifically remain the biggest sticking points. In the January data, shelter, which represents 35% of the index, was up 0.4% MoM and 4.4% YoY. More broadly, service (representing almost two-thirds of CPI) was up 4.2% YoY while commodities less food and energy (20% of the index) were negative from a year earlier. The stubborn inflation will likely make the Fed less likely to cut rates and adopt a patient, wait-and-see approach. After the January price data, futures now indicate equal odds of one or two interest-rate cuts total (25 basis points each) for calendar-year 2025.

Consumer Price Index (Core and Overall) vs. 2% Target



As of January 31, 2025
Source: Haver

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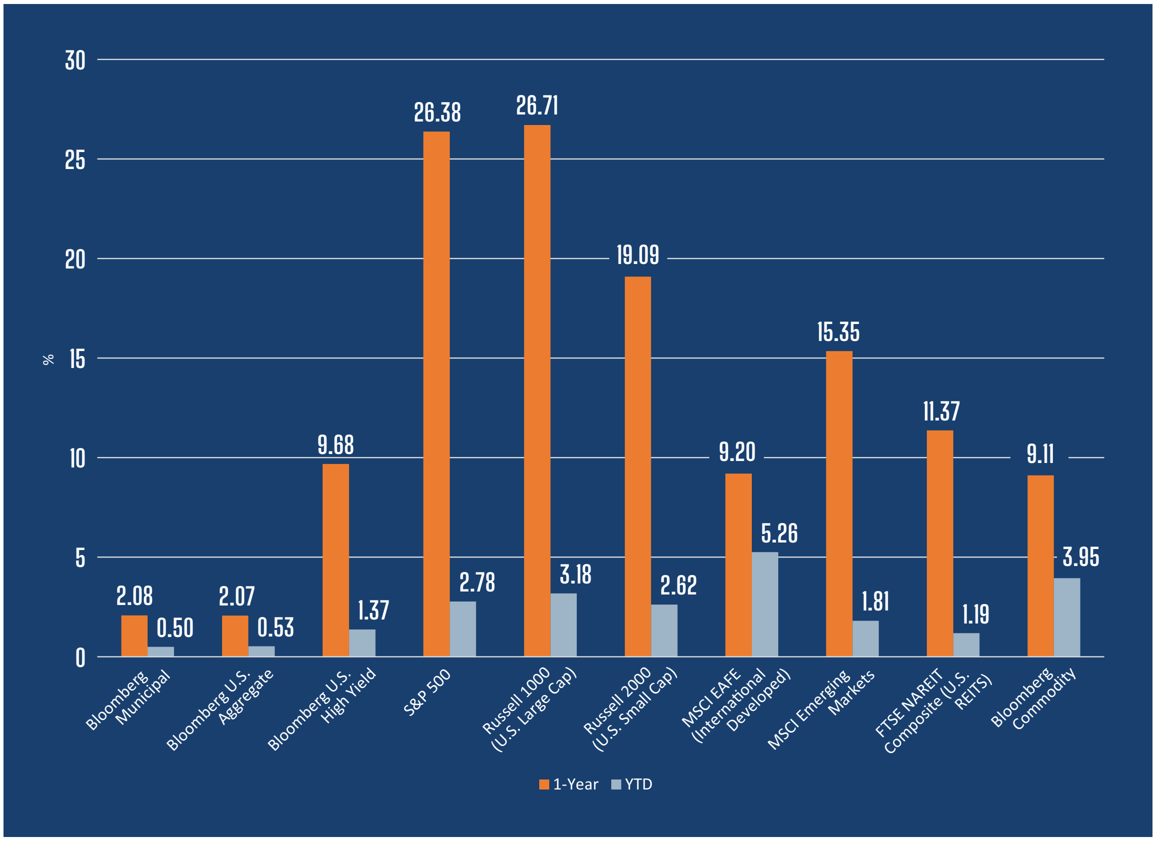
Asset Class Returns

Comparing Recent 1-Year and Year-to-Date Total Returns



As of January 31, 2025
Source: Conway Investment Research

Fixed Income

- The decline in Treasury and other sovereign debt yields provided another strong month of performance for fixed income across the globe.
- Core fixed income and municipals generated very solid performance while most areas of credit benefited from higher carry/ starting yields.
- After being negative for most of the year, the Bloomberg Aggregate Index is now up over 3%.
- Bonds outside the United States also received a boost from the weaker U.S. dollar.

Equities

- U.S. equities were a mixed bag in August with gains in large caps and weakness across small caps.
- Value beat growth within large caps, but the opposite occurred within small caps.
- The S&P 500 has gained 19.5% in 2024, and the Russell 2000 is up 10.4%.
- Equities outside the United States generally gained ground and outperformed U.S. equities last month. U.S. dollar weakness provided an added tailwind to non-U.S. assets.
- Unlike what occurred in the United States, growth beat value across EAFE equities.
- Emerging markets lagged developed markets in August, driven mainly by ongoing weakness and poor sentiment in Chinese equities.

Alternatives

- Real estate investment trusts, or REITs, posted another strong month as rates fell.
- Commodity prices were flat with gas and oil noticeably weaker.

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January 31, 2025	MTD	QTD	YTD	1-Year	3-Year	5-Year	10-Year
Fixed Income Indices							
Bloomberg U.S. Treasury Bill 1-3 Month	0.37%	0.37%	0.37%	5.25%	4.11%	2.54%	1.79%
Bloomberg Municipal	0.50%	0.50%	0.50%	2.08%	0.54%	0.73%	2.12%
Bloomberg US Govt/Credit Intermediate	0.46%	0.46%	0.46%	4.43%	2.08%	1.56%	1.62%
Bloomberg U.S. Aggregate	0.53%	0.53%	0.53%	2.07%	-1.52%	-0.60%	1.19%
Bloomberg U.S. High Yield	1.37%	1.37%	1.37%	9.68%	4.34%	4.49%	5.24%
Bloomberg Global Aggregate	0.57%	0.57%	0.57%	0.25%	-3.68%	-2.10%	0.22%
U.S. Equity Indices							
DJ Industrial Average	4.78%	4.78%	4.78%	18.93%	10.45%	11.79%	12.50%
S&P 500	2.78%	2.78%	2.78%	26.38%	11.91%	15.17%	13.76%
NASDAQ Composite (Price)	1.64%	1.64%	1.64%	29.43%	11.29%	16.49%	15.53%
Russell 1000	3.18%	3.18%	3.18%	26.71%	11.69%	14.97%	13.54%
Russell 1000 Growth	1.98%	1.98%	1.98%	32.68%	14.57%	18.90%	17.18%
Russell 1000 Value	4.63%	4.63%	4.63%	19.54%	8.08%	10.15%	9.42%
Russell Mid Cap	4.25%	4.25%	4.25%	21.99%	7.96%	11.02%	10.26%
Russell 2500	3.54%	3.54%	3.54%	19.08%	6.63%	9.98%	9.45%
Russell 2000	2.62%	2.62%	2.62%	19.09%	5.62%	8.67%	8.45%
Russell 2000 Growth	3.16%	3.16%	3.16%	22.73%	6.23%	7.76%	8.68%
Russell 2000 Value	2.05%	2.05%	2.05%	15.52%	4.71%	8.93%	7.82%
Non-U.S. Equity Indices							
MSCI World	3.55%	3.55%	3.55%	21.94%	10.07%	12.61%	11.11%
MSCI ACWI	3.38%	3.38%	3.38%	21.27%	8.93%	11.56%	10.32%
MSCI ACWI Ex-U.S.	4.05%	4.05%	4.05%	11.48%	3.99%	6.02%	5.74%
MSCI EAFE	5.26%	5.26%	5.26%	9.20%	5.66%	6.77%	6.20%
MSCI EAFE Growth	5.41%	5.41%	5.41%	6.64%	3.21%	5.56%	6.65%
MSCI EAFE Value	5.12%	5.12%	5.12%	11.94%	8.03%	7.62%	5.51%
MSCI Europe	6.90%	6.90%	6.90%	9.61%	5.77%	7.49%	6.32%
MSCI Japan	1.57%	1.57%	1.57%	5.51%	5.53%	5.81%	6.54%
MSCI AC Asia	1.05%	1.05%	1.05%	14.20%	2.07%	4.62%	5.44%
MSCI EAFE Small Cap	3.45%	3.45%	3.45%	7.62%	0.85%	4.05%	6.29%
MSCI ACWI Ex-U.S. Small Cap	1.35%	1.35%	1.35%	7.08%	1.62%	5.71%	6.28%
MSCI Emerging Markets	1.81%	1.81%	1.81%	15.35%	-0.26%	3.45%	4.16%
MSCI EM Asia	0.76%	0.76%	0.76%	19.65%	0.24%	4.52%	5.02%
MSCI China	0.95%	0.95%	0.95%	35.16%	-4.68%	-2.15%	1.92%
MSCI EM Eastern Europe	12.39%	12.39%	12.39%	14.10%	-31.74%	-20.11%	-4.09%
MSCI EM Latin America	9.54%	9.54%	9.54%	-14.89%	3.34%	0.03%	2.32%
MSCI EM Small Cap	-2.76%	-2.76%	-2.76%	4.11%	3.19%	9.33%	5.69%
MSCI Frontier Markets	3.03%	3.03%	3.03%	12.13%	-0.88%	2.79%	3.35%
Hedge Fund Indices							
IQ Hedge Multi-Strategy	1.77%	1.77%	1.77%	9.77%	4.37%	3.62%	3.09%
Real Assets Indices							
FTSE NAREIT Composite	1.19%	1.19%	1.19%	11.37%	-1.35%	2.85%	5.19%
Alerian MLP	8.79%	8.79%	8.79%	29.61%	26.39%	18.88%	4.87%
Bloomberg Commodity	3.95%	3.95%	3.95%	9.11%	2.49%	9.25%	2.02%
S&P Global Infrastructure	2.30%	2.30%	2.30%	21.57%	8.23%	5.42%	6.15%
Other							
Oil Price Brent Crude	3.58%	3.58%	3.58%	-6.40%	-5.70%	5.63%	3.74%
CBOE Market Volitility (VIX)	-5.30%	-5.30%	-5.30%	14.49%	-12.86%	-2.70%	-2.41%

Source: Morningstar

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The return of principal for bond funds and funds with significant underlying bond holdings is not guaranteed. Fund shares are subject to the same interest rate, inflation and credit risks associated with the underlying bond holdings. Lower rated bonds are subject to greater fluctuations in value and risk of loss of income and principal than higher rated bonds. Bond prices fluctuate inversely to changes in interest rates. Therefore, a general rise in interest rates can result in the decline of the value in your investment.

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