TARIFF TURMOIL: OBSERVATIONS AND ADVICE

APRIL 7, 2025

Cutting through the "noise" during times of high market volatility can be challenging but this piece attempts to do so by offering our perspective concerning recent market events, some historical context, and a few forward thoughts. Appleton's Wealth Managers are available to discuss your personal circumstances, so please reach out.

Global Trade Relations Rocked by Tariff Announcements

While it was widely expected that the second Trump Administration would take a hawkish stance on trade policy, expectations of modest tariffs increases used primarily as negotiating tools appear to have been overly optimistic. Using a controversial interpretation of emergency economic powers, **April 2nd's announcement of a universal 10% tariff coupled with individual "reciprocal tariffs" stunned markets, leading to a rapid and pronounced stock market slide**.

Fed Chairman Powell emphasized on April 4th that the proposed tariffs were "significantly larger than expected" and will probably lead to "at least a temporary rise in inflation." According to Strategas, the announced tariffs amount to 2.2% of GDP and are effectively twice the size of the largest tax increase in modern US history.

Isaac Newton long ago stressed that "for every action, there is an equal and opposite reaction." While his findings led to breakthroughs in physics, not economics, there is a good deal of market applicability. An onerous 34% rate assessed on Chinese imports was quickly matched by China, a move some believe was designed to pressure US markets and policymakers. As we write, there are reports of possible further increases in Chinese goods if their retaliation is not rescinded, suggestions that the EU will soon vote on retaliatory measures, and suffice it to say, other countries are considering their own responses. **Forcing trade partners to the table may be an Administration objective, but it creates a great deal of uncertainty that markets have difficulty pricing.**

Initial Economic and Market Reaction

The last few days have produced a painful "risk-off" reaction with the S&P 500 posting -4.8% and -6.0% days to close last week's trading, shedding $6.6 trillion in value. This was the sharpest 2-day fall since the onset of COVID in March 2020, and further declines have been incurred so far during April 7th trading.

As might be expected, a flight-to-quality has driven high-grade bond prices up and yields down with the 10Yr UST falling 37bps to 4.00% in only 6 trading days, and 5-year AAA municipal yields declining to 2.59%. It is noteworthy that **high quality bonds have buffered equity volatility to a degree, benefiting investors in balanced strategies and offering a reminder of the benefits of asset class diversification.**

Tariffs are likely to reduce corporate profits and/or be inflationary as import costs are often passed on to consumers. **Business and consumer sentiment has at least temporarily been shaken**, as evidenced by falling confidence readings and C-Suite surveys, while the potential for recession is increasing.

Where Do Things Go From Here?

The White House is holding firm, and the President and top aides took a hawkish tone over the weekend, expressing a view that "sometimes you have to take medicine," and that their policy is long-term in nature. On the negotiating front, the Administration is stressing that dozens of countries have reached out to initiate tariff talks. How much dialogue is actually taking place is not known, although the importance of the US market creates significant leverage.

Behind the scenes, there are also signs of GOP anxiety relative to the severity of the President's trade stance. Rectifying what he sees as "bad trade deals" and "unfair trade practices" has long been a policy objective, although what constitutes "victory" and a trigger to roll back certain tariffs is an open question.

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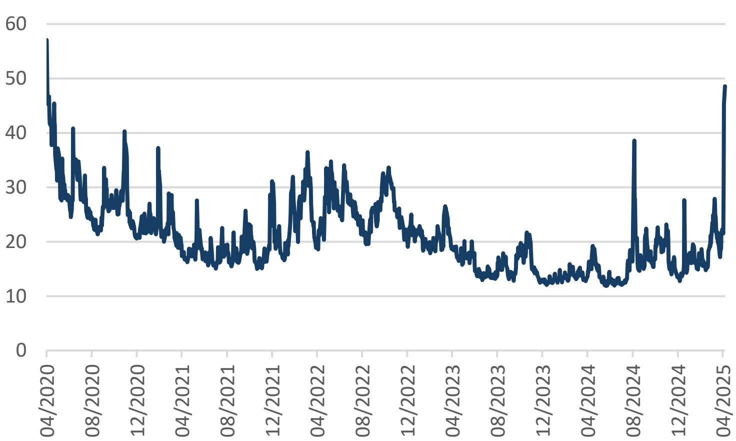
Street consensus now calls for a 35-45% chance of a 2025 recession. Should one occur, its length and depth is likely to be influenced by how trade negotiations play out, as well as the extent to which offsetting fiscal and monetary policy measures are able to ease trade-related economic impact. Maintaining announced tariff levels without offsetting policy measures to benefit the economy would significantly increase recession risk. To that end, **Republicans in Congress are under pressure to fast-track extension of the 2017 TCJA tax cuts while also introducing wider deregulation to jumpstart growth and forestall a potential downturn.** We anticipate developments on this front over the next few months.

Unfortunately, it does not appear that the Fed will be immediately riding to the rescue. Chairman Powell's weekend comments threw cold water on the notion of rapid easing as he emphasized their inflation control mandate. Our sense is that they will evaluate forthcoming CPI and PPI prints, business and consumer sentiment, and other economic factors in weighing the balance of inflation and growth risks. **Easing later in the year is anticipated though and Fed funds futures are pricing in 80bps by the end of Q3. This, coupled with a calming of trade tensions and/or an extension of tax cuts, would likely be positive stock market catalysts.**

The VIX, an index measure of volatility, surged to more than 60 on April 7th, far above the 5-year average of 20.7. History offers cause for optimism though, as past periods of extreme volatility have often led to strong forward returns. This speaks to a tendency for markets to bounce back forcefully when sentiment changes, particularly after periods of intense selling. The accompanying chart from Charlie Bilello of Creative Planning details the extent to which investors have been rewarded for staying the course. Reacting emotionally and arbitrarily selling while under stress can harm long-term capital growth should investors miss a subsequent recovery rally.

Market Volatility Spikes on Tariff Turmoil
(VIX Index Reading)



Source: Bloomberg

Biggest Weekly $VIX Spikes and Forward S&P 500 Total Returns (January 1990 - April 2025)								
Biggest 1-Week $VIX Spikes				Forward S&P 500 Total Returns				
End Week	Start $VIX	End $VIX	$VIX Spike	1-Year	2-Year	3-Year	4-Year	5-Year
2/28/2020	17.08	40.11	135%	31.3%	53.2%	41.0%	83.7%	120.0%
8/21/2015	12.83	28.03	118%	13.3%	28.4%	53.8%	59.1%	89.4%
4/4/2025	**21.65**	**45.31**	**109%**					
5/7/2010	22.05	40.95	86%	23.0%	28.4%	54.9%	84.3%	110.8%
12/12/2014	11.82	21.08	78%	2.6%	17.8%	41.0%	42.8%	74.0%
3/2/2007	10.58	18.61	76%	-2.2%	-44.6%	-14.9%	3.8%	9.6%
2/9/2018	17.31	29.06	68%	5.4%	32.1%	57.1%	84.5%	72.4%
12/11/2015	14.81	24.39	65%	14.8%	37.4%	39.1%	69.6%	103.1%
11/26/2021	17.91	28.62	60%	-11.0%	2.5%	36.1%		
3/23/2018	15.80	24.87	57%	10.4%	-7.3%	60.0%	85.1%	65.2%
2/2/2018	11.08	17.31	56%	-0.1%	21.5%	42.4%	72.4%	60.9%
10/10/2008	45.14	69.95	55%	22.3%	35.8%	37.4%	77.6%	110.0%
8/11/2017	10.03	15.51	55%	18.3%	24.3%	45.6%	95.7%	85.5%
2/4/1994	9.94	15.25	53%	4.8%	42.8%	80.4%	128.9%	203.3%
1/22/2010	17.91	27.31	52%	19.9%	25.5%	45.0%	83.3%	105.5%
10/31/1997	23.17	35.09	51%	22.0%	53.3%	57.0%	27.3%	5.0%
1/29/2021	21.91	33.09	51%	21.0%	13.0%	38.0%	74.5%	
1/21/2022	19.19	28.85	50%	-8.2%	13.7%	42.8%		
4/1/1994	13.67	20.45	50%	15.6%	52.7%	87.0%	169.2%	219.8%
9/6/2024	15.00	22.38	49%					
Average (20 Biggest 1-Week Spikes)				11.3%	23.9%	46.9%	77.6%	95.6%
Average All Other Periods				12.1%	25.2%	39.2%	55.8%	73.9%
Differential				-0.8%	-1.3%	7.7%	21.8%	21.8%
CREATIVE PLANNING				@CharlieBilello				

Source: Creative Planning, Charlie Bilello

Back to the Basics

Fundamentals always matter, particularly during stressful and uncertain times. **Over the long term, corporate earnings drive stock prices.** The S&P 500's value has demonstrated an exceptionally high 0.97 correlation with S&P 500 earnings growth since 1957 according to Bloomberg data cited by Invesco. Consensus 2025 S&P 500 earnings growth estimates have come down to about +11% and are falling further, while Q1 projections appear to center around +4%. We are carefully evaluating the profit outlook of the companies owned in Appleton client portfolios, as well as those we are considering adding. **If management guidance is not overly cloudy and earnings can remain solidly positive, recent sell-off induced valuation reductions make the forward outlook more appealing.**

As we always emphasize, a personalized, risk managed asset allocation strategy is designed in part to allow investors to more comfortably stay the course during challenging times. While doing so can sometimes be emotionally taxing, **market timing has long proven to be extraordinarily difficult and is not recommended.**

APPLETON PARTNERS, INC.

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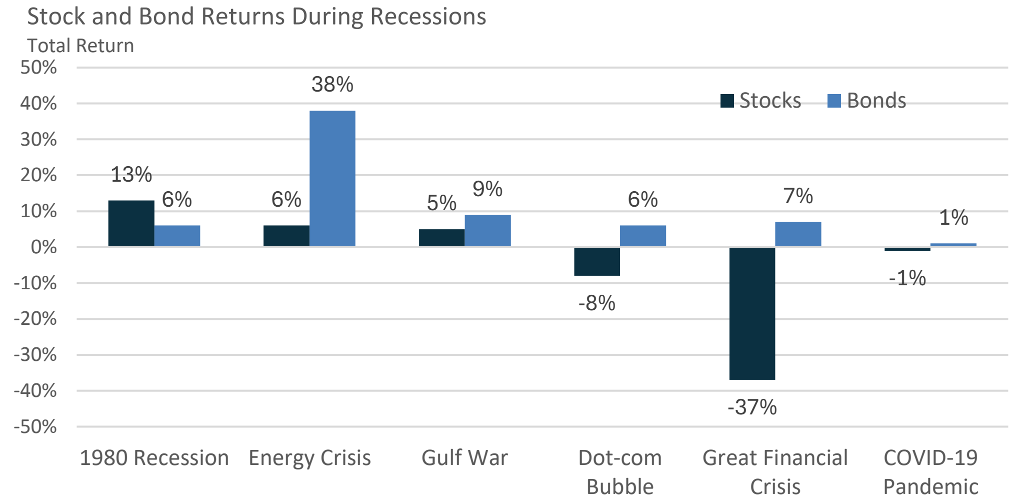
We recognize that it doesn't feel good right now, but if past is prologue, maintaining a risk compatible level of equity exposure should be beneficial longer term. **Stock market losses have typically been relatively short-lived, and rebounds pronounced.** Since 1945, there have been 15 declines of -10 to -20% and the average recovery time has been only 8 months, a modest price to pay for the compound effect of long-term growth in capital (FactSet, Dow Jones).



Source: JPMorgan's Guide to the Market, April 4, 2025

Our Equity and Fixed Income teams look at dislocations with a cautious yet opportunistic eye, and are actively engaged in economic, market and security specific analysis with an eye towards identifying investment value. Right now, we are looking to add exposure in quality defensive stocks with less than average tariff exposure that we feel offer attractive relative value.

It can understandably be difficult to avoid overreacting to disconcerting headlines, although we strongly advise stepping back and staying calm. Reassessing one's risk tolerance as needed and considering time horizon before making any investment decisions is recommended.

Accessibility and communication are important in any environment, although these attributes are especially valuable during uncertain and volatile times. Appleton Partners is committed to sharing our market and portfolio management perspectives as developments unfold. We hope these briefs are helpful and also invite you to reach out to us directly and/or visit www.appletonpartners.com/Insights for additional commentary and insights.

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