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QUARTERLY COMMENTARY

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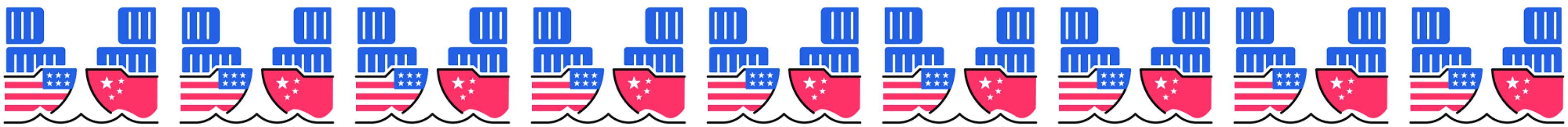
Tariffic Times

How markets perform this year is ultimately up to one man – our friendly neighbour to the south, Mr. Donald Trump. While many very smart business people assumed that his administration would lead to lower taxation, less bureaucracy and greater wealth, it seems that the opposite is coming to fruition. Trump's obsession with using tariffs to fix something that truly ain't broken with the goal of increasing America's wealth is causing worldwide havoc and threatening major recessions and a global slowdown. All this while the wealthiest country in the world was actually doing quite well, thank you (4% unemployment, strong corporate profitability, 2.4% GDP growth in the fourth quarter of last year). Of course, there's nothing wrong with trying to improve America's trade imbalance (especially with China) but the manner in which it's done is paramount. The problem with Trump's bullying approach is simple – he's attempting to run the country in the same manner he ran his property development business. International trade however is nothing like negotiating supply agreements for construction projects.

Professor David Honig of Indiana University explains in elegant terms the inappropriateness of Trumps negotiating style. In Trump's world you are either a winner or a loser - the fight is over a piece of the pie and whoever gets the biggest piece wins. It's called distributive bargaining which happens when there is a fixed quantity of something two sides are fighting over – the more he gets or saves the more he wins. The other type of bargaining is called integrative bargaining in which the two sides don't have a complete conflict of interest and it's possible to reach mutually beneficial agreements – like a baker and a caterer deciding how many pies will be baked, at what prices, and the nature of their ongoing relationship after the one contract is completed. Trump's problem is that he only uses distributive bargaining in an international world that requires the integrative approach. He can increase tariffs, but so can other countries – he can't demand that they don't respond and there is no simple winner and loser because there are always more pies to be baked for other customers. China's choice isn't to buy soybeans from US farmers or don't buy soybeans at all. They can also buy soybeans from Russia, Argentina, Brazil, Canada etc… It completely strips the distributive bargainer of his power to control the negotiation. Of course – that's not to say that most countries (not China though) won't attempt to play his game in order to appease him. But with his hammer-over-the-head style a major risk is bad will – a credibility vacuum so vast that America's reputation goes down the drain. Doesn't Canada already have a free trade agreement with America – crafted by his own administration last time around? One that he raged against in March after having bragged about it when it was completed as being "the best and most important trade deal ever made by the USA". With international negotiations in a complex world, integrated economies and multiple buyers and sellers, there is little chance for success with his approach. You can't possibly succeed by bullying China (Xi cannot be seen as submitting to US demands) and so the world's largest two-way trade relationship (the US imported $440 Billion worth of Chinese goods last year – more than three times the $144 Billion of US goods that China imported) is at risk and so is the global economy.

The concern is not just a dent in global growth but also a move towards protectionist policies that drive up inflation, sap corporate profits and chill investment – a possible new era for global business. There is a glimmer of hope though as President Trump has finally listened to some of his billionaire backers like Bill Ackman (who said there would be an "economic nuclear winter") as well as Jaime Dimon and many high tech CEOs who no doubt pressured him to back track from his original position.

He has now proclaimed a 90 day reprieve and an exclusion for high tech products. This is a major about-face which has greatly relieved the markets in the very short term. Hopefully Trump will be able to also claim some victories and then reverse course even further from what could be a critical turning point in trade relations around the world. Certainly Canada’s relationship with America is permanently harmed. Yet in the long run, it will be to our benefit because we’ve relied way too heavily on trade with our southern neighbour. It was about time we diversified our economic relationships and looked elsewhere to enhance our economic independence.



The first quarter of 2025 was a mixed one with regard to investment performance. The Canadian market return was 0.7%, the S&P500 stumbled down 4.6% after a terrific 2024, and Emerging Market equities outperformed developed markets, with Chinese and Korean equities both performing strongly. Value stocks outperformed their growth counterparts, while smaller companies lagged, returning -3.6%, as rising trade uncertainty drove concerns around both weaker growth and stronger inflation. Bonds were up around 2% but commodities were by far the top performer over the quarter, boosted by a 19% rise in gold prices. As I write and as I outlined in last quarter’s newsletter, volatility has returned with a vengeance with the largest two day drop in the equity markets in over five years in the first week of April. I expect it will continue to be challenging – especially the next six months or at least until such time that we get more clarity on how Trump’s big gambles pay off. Between Washington’s unpredictability and the China tariffs escalation, the market can easily continue to whipsaw back and forth. In our discretionary portfolios in order to manage through these difficult market conditions we've maintained a higher than usual cash weighting, profited from the rise in gold, and rebalanced portfolios. High quality stocks like Royal Bank, Enbridge, Emera, and Dollarama are all great companies and remain core holdings. So, in short, we adhere to our discipline and will use the cash when opportunities present themselves to reposition our weights in companies that we believe will benefit once markets move past this period of heightened uncertainty. 'Winter will be forced to relent, once again to the new beginnings of soft greens, longer light and the sweet air of spring.' Madeleine M Kunin

As always if you have any questions, are interested in a particular investment or you would like to have a comprehensive financial plan created for you please don't hesitate to call. In the meantime, enjoy the spring!

Regards,

Richard