

**H. Terrence Riley III, CFA**  
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**Contact: Karin Müller-Paris**  
**+1-561-208-1081 [kmm@fvcm.us](mailto:kmm@fvcm.us)**



## Trump’s Tariff Policy Worse Than Expected

**Yesterday, Trump announced a 10% across the board tariff on all imports to the U.S., and higher “reciprocal” tariffs on specific countries.** It is still not totally clear how the multiple tariffs tally up, but the additional reciprocal tariffs will be applied on 60 nations including a 34% tariff on China, 32% on Taiwan, 46% tariff on Vietnam, and 20% on the EU. Canada and Mexico also have a 25% tariff, although imports that are compliant with the USMCA trade agreement with those two countries are exempt. Trump has said that his tariff actions reflect alleged non-tariff barriers, such as currency manipulation, VAT, and environmental impacts. Days earlier, a nearly 400-page report was released that detailed Foreign Trade Barriers which can be found by googling [2025NTE.pdf](#).

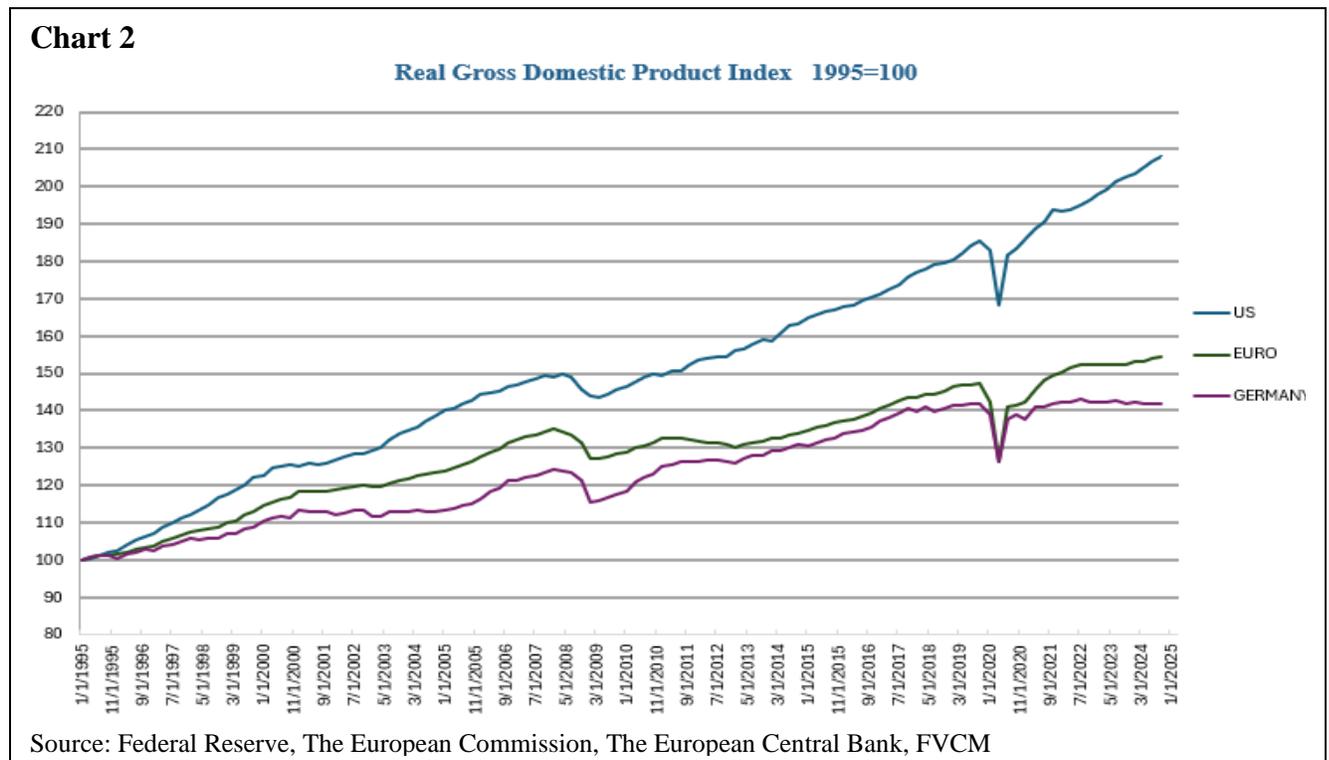
**These actions are unprecedented in modern times and are at odds with classical economic thought and literature.** The famous Scottish philosopher, Adam Smith, known as the father of economics, said *"nothing, however, can be more absurd than this whole doctrine of the balance of trade."* Politicians worldwide have long pandered for votes by providing trade protections to favored groups like farmers and auto manufacturers. Smith's idea was that free trade resulted in the greatest efficiency and human prosperity. Furthermore, imports are the greatest benefit to a nation, not exports. Isn't the age-old criticism of colonialism that the colonial powers conquered foreign nations to gain access to their raw materials and goods to ship back to the mother country? No one ever criticized the colonialists because they put all their production on ships to send to primitive foreign lands, because the idea of prosperity resulting from exporting your production is absurd. A nation only exports its production for sale so that it can buy production from other lands to bring back home. Trade deficits reflect timing decisions to invest export proceeds in the importing country rather than immediately purchase tradable goods for shipment back home. Just imagine if there were only two countries—the U.S. and Japan. If Japan sent large ships filled with Japanese built Toyotas to the U.S., and never, not in a thousand years, had anything shipped back to Japan except pieces of paper with U.S. presidents on it, which nation most benefited from trade?

**The outlook for the U.S. economic growth for 2025 has now worsened. Thus far, median GDP growth forecasts have fallen 0.4% to 1.7% (growth was 2.8% in 2024), and estimates are likely to fall further.** Wall Street market strategists are also cutting expectations for corporate earnings. After all, some 40% of the sales for the S&P 500 are derived from business overseas, and companies like Apple, which has nearly all of its manufacturing in Asia, will have big hits to profit margins from the tariffs. Bank of America strategists estimated that profits for the S&P 500 could be negatively impacted between 5% and 35%. J.P. Morgan economists said the tariffs could raise inflation by between 1% to 1.5% this year and cause real disposable income to decline. For mathematical reasons, there had been speculation that tariffs would cause the dollar to strengthen, but we actually saw the dollar weaken in reaction to the tariffs because of the risk to growth.

**How this "tariff war" plays out, and its ultimate effect on the economy and business, remains cloaked in tremendous uncertainty.** Some countries like Australia and Mexico have indicated that they will not retaliate—at least for now. The French, who always seem to enjoy brazen talk about wars—even trade wars, are ready to push the EU to retaliate against the Trump tariffs immediately. The damage that is inflicted on the U.S. and global economy will ultimately depend on foreign reaction to Trump's tariffs, as well as Trump's willingness to back away from the edge of the cliff as trade negotiations proceed. No one knows but we are hopeful because the market reaction has been immediate and should be startling even to those in the administration that support the tariffs.

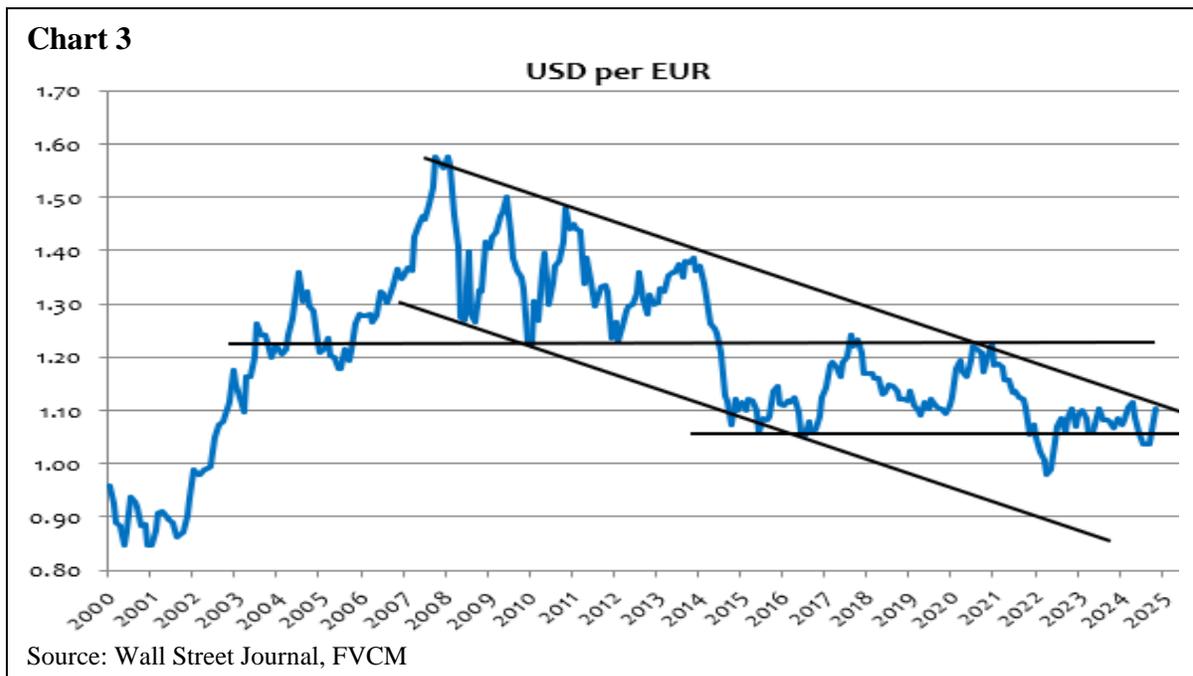
**A trade war started by the U.S., such that there is one, seems odd because there is data that supports the idea of American exceptionalism.** As shown below in Chart 2, the U.S. economy has far outgrown Europe and Germany over the past thirty years. There are many reasons for this divergence, but here are a few:

1. The U.S. has highly developed capital markets, paired with an entrepreneurial spirit. "Innovative companies that want to scale up in Europe are hindered at every stage by the lack of a Single Market and an integrated capital market, stopping the cycle of innovation in its tracks. As a result, many European entrepreneurs prefer to seek financing from U.S. venture capitalists and scale up in the U.S. market." - Mario Draghi 2024.
2. The U.S. has lower energy costs. European industrial energy (the lifeblood of an economy) costs almost 3x more than industrial energy in the United States. This divergence began in the late 1990's and has since accelerated.
3. The U.S. has more business-friendly tax, labor and regulatory policies. The European regulatory environment surrounding big tech and AI is simply the latest in a series of anti-business actions taken by Europe in recent decades.



**As for the equity markets, it would appear that the horses have already passed the gate and it's late to be selling stock at this point.** Stock prices peaked in mid-February. The Nasdaq 100, which is heavily weighted with the so-called magnificent seven and other big tech stocks, was already in correction territory, i.e., down more than 10%, by March 10<sup>th</sup>. With Trump's tariff announcement out, that index is now down some 16%. The S&P 500 has been slower to correct and is now down about 11% from the peak in February. There is no scientific evidence to tell us when stock prices will begin to rebound, but many technical indicators suggest that a bounce may be near. Sentiment indicators have turned very negative, which means that the market emotions are overdone. Also, looking at the chart on page one, momentum indicators like the 14-day RSI, now at 33, are approaching oversold levels. More importantly, there are some fundamental positives to consider:

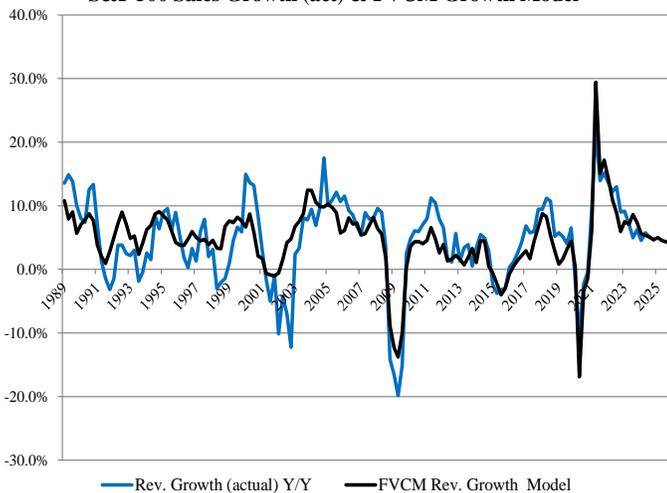
1. Trump's rapid action to reduce government expenditures and regulations will have material positive impact on the Federal budget and private industry. These factors should mitigate some of the damage from the tariffs.
2. The Euro at 1.11 is hitting a resistance level in its long-term downtrend and the dollar may begin to strengthen again (see Chart 3 below). For mechanical and mathematical reasons, the consensus had been that Trump's tariffs would cause the dollar to strengthen. This has not been the case in recent days because of concerns, which we have discussed, that the tariffs would cause growth to slow.



- The consensus forecast is still close to 2%, but U.S. real GDP growth will likely to be not more than 1.5% in 2025, down from 2.8% in 2024. Note: our models use 4.7% nominal GDP growth for '25, versus 5.3% in '24.
- As shown in chart below, based on our expectations for nominal GDP growth and a relatively stable F/X rate, sales for the S&P 500 are forecasted to increase a moderate 4.5% in 2025.
- Net profit margins are now flattening out. Our models indicate increases of 4.9% and 5.5%, respectively, in operating earnings and GAAP earnings for the S&P 500 in 2025, versus 2024. However, our model does not account for the tariffs. Hence, we think earnings could end up being between -5% and flat for 2025.
- With the S&P 500 now trading at about 23 times the '25 estimate of flat operating earnings, valuations are high. However, the U.S. is going through generational change and rising productivity, and growth could reaccelerate in '26 after the Trump transition settles down. At current prices, we are holding stocks that are reasonably valued, but not adding to positions just yet. But we are looking at these lower prices as an opportunity to be buyers of stock that we previously thought too expensive.

**Chart 4**

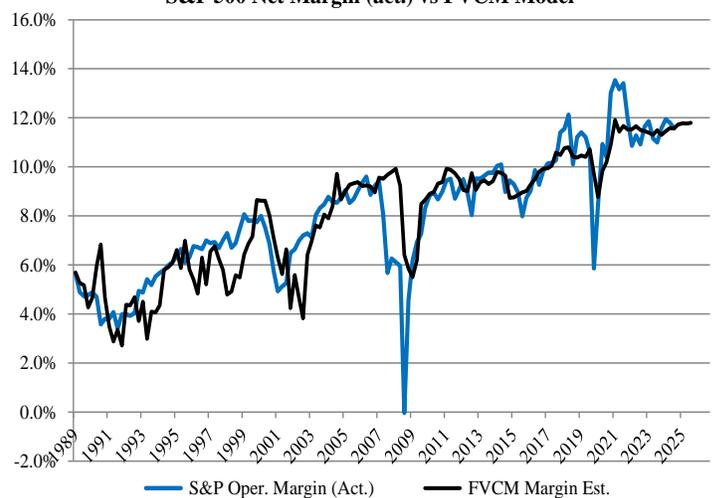
**S&P 500 Sales Growth (act) & FVCM Growth Model**



Source: S&P Global, FVCM

**Chart 5**

**S&P 500 Net Margin (act.) vs FVCM Model**



Source: S&P Global, FVCM

**In summary, Trump’s tariff policy, such as we now understand it, is worse than expected and a significant negative factor for both U.S. and global growth, but the possibility exists that most U.S. trading partners will react in a constructive way, and the impulsive Mr. Trump will soon dismiss some of these actions.** Stock investments are notoriously difficult because traders often act by selling after negative factors become known. It thus becomes easy to get whipsawed by a rebounding market. At this stage of perception, investors may be rewarded by standing aside a bit longer to allow some smoke to clear. The U.S. is a large and compelling market for long-term equity investors. Lower stock prices make stock purchases more attractive, not less. Timing is never perfect, but opportunities lie ahead.

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