Sage Advisors

MassMutual

Market Update
April 4, 2025
Courtesy of Sage Advisors

Let us imagine there are two countries. Country A is large, mostly meadows and wide-open fields. They have plenty of fresh water and a hard-working and diligent populace. Much smaller, Country B is an island with rocky terrain. Its people are clever, resilient, and renowned for their fishing and aquatic skills.

Country A produces wheat, corn, and other agricultural products. In addition, they use those harvests to raise various meat products, such as beef and pork. Country B uses their abundant resource to catch and farm fish and produce a number of ancillary products. Country A can catch the occasional fish, but it's challenging and not particularly abundant. Country B has tried to grow various grains, but the salty air tends to destroy their crops, and the occasional large storms tend to erode their progress.

One day, someone from Country A visits Country B and is impressed with the quality and abundance of fish. They agree to trade a certain amount of wheat and grain from Country A for fish from Country B, to be delivered monthly. Both parties are happy, and both countries are better off.

That, ladies and gentlemen, is the essence of free trade. Both countries benefit. This dynamic exists because resources such as geology, topography, climate, labor, and skill vary from country to country. It's driven a move toward globalization for the past 200 years and accelerated over the last 80 years.

On April 2, that all changed through the most impactful and significant free trade disruption in at least 50 years.

What follows is a (hopefully) bipartisan attempt to explore what has happened, why this is occurring, and where we are going from here. With that, let us begin.

Uncertainty, Ugliness, and Uggh

First, if you are avid readers of these updates, you will note we walked through a primer on tariffs in the March 10 update. If you have not read that update, I suggest you do so now.

Second, if you understand tariffs, let us move to the play-by-play of what has occurred in the past couple of months:

Jan. 14: President-elect Trump announces plans to create the External Revenue Service to manage tariffs and duties from foreign sources. He plans to establish this agency on Jan. 20, upon taking office for his second term.

Jan. 26: The U.S. avoids a trade war with Colombia after the country agrees to accept military aircraft carrying deported migrants. Trump had previously threatened tariffs and sanctions due to Colombia's initial refusal.

Feb. 1: Trump declares a national emergency over illegal immigration and drug trafficking, including fentanyl. He imposes:

- 25% tariffs on imports from Canada and Mexico
- 10% tariffs on imports from China
- 10% tariffs on Canadian energy resources

Feb. 3: Trump delays the newly announced 25% tariffs on Canada and Mexico for one month after both countries agree to enhance border security.

Feb. 7: Trump postpones tariffs on low-cost (de minimis) packages from China until the Commerce Department ensures systems are in place to process packages and collect revenue.

Feb. 10: Trump says he will postpone a 25% tariff on steel and aluminum imports.

March 4: The Trump administration enacts previously delayed tariffs on Canada and Mexico, imposing a 25% levy on all imports from both nations. The president also adds an additional 10% tariff on all imports from China.

March 6: Trump pauses many tariffs on Canada and Mexico for one month, but only goods covered under the U.S.-Mexico-Canada Agreement (USMCA) are exempted from tariffs.

March 12: The Trump administration increases tariffs on steel and aluminum imports to 25% globally (up from the original 10%).

March 31: The administration establishes the United States Investment Accelerator within the Commerce Department to expedite domestic corporate investments.

April 2: President Trump declares April 2 as Liberation Day announcing:

- A universal 10% tariff on all goods coming into the United States, effective April 5
- "Reciprocal tariffs" targeting countries with significant trade surpluses with the U.S., including:
    - China: 34% total tariff
    - Taiwan: 32% total tariff
    - Japan: 24% total tariff
    - European Union: 20% total tariff

Which brings us to present day, where the Standard & Poor's (S&P) 500 has lost nearly 9% of its value in 48 hours, a collection of indices has lost nearly $8 trillion, and many indices are now in official "corrections."

For some perspective, I bring you to Chart 1, which shows the average tariff rate on all imports into the United States.

Chart 1: Average Tariff Rate on U.S. Imports[1]

Wait, but Why?

If you are of the unlucky cohort that opened your account statements today, very quickly you will ask (after your eyes recover from seeing so much red), but why? Things were great, you'll say! Markets were strong in 2023. In 2024, my portfolio was growing. Why would a president do something of this sort? Six months ago, the United States was in the enviable position of strong growth, low unemployment, and very strong capital markets.

The answer is pretty straightforward. For a moment, ignore all you are reading and turn off the news channels.

The administration is clear about what it wants and, whether you agree with those goals or not, it is pursuing those objectives at unprecedented speed.

1) The Trump Administration wants to build back the **U.S. manufacturing sector**. While there are multiple reasons, defense and economic sovereignty are clearly the top two.

2) The second goal is to reduce the **trade deficit**. The U.S. business model (as discussed here before, somewhat tongue in cheek) has been to import goods and export bonds. Said another way, each year, we have generally imported far more goods than we have exported, and we have paid for that difference by selling bonds.

[1] Source: Bloomberg, WMIT, taxfoundation.org, through Aug. 20, 2024

If you haven't read President Trump's executive order[2], I encourage you to do so. The Trump Administration is quite clear about its views. To harken back to our two-country example, the administration is moving away from free trade and prefers, instead, to enable Country A to produce and consume much of what they need themselves. Whether you agree, it is clear that this is the goal.

Do We Care?

Aside from the obvious "markets are down, which hurts" perspective…the next question I hear often is "well, why do we care?"

In a nutshell, such extreme tariffs:

1) Hurt growth
2) Raise prices
3) Create uncertainty

The net result is a dramatic increase in the likelihood of a recession.

As mentioned before, tariffs aren't necessarily "bad" or "good," they are simply a tool. Tariffs announced in such a rapid and extreme fashion, however, cause massive uncertainty and do so in an unnecessarily condensed time period.

Companies around the world right now are in panic mode. "Should we move factories?" "Should we wait to see if the tariffs are reversed?" "Will other countries retaliate?" "Should we find new suppliers?"

Investors around the world are furiously trying to determine how this will play out and, for global investors at least, all they are certain of is that everything has changed—overnight.

What's Next?

First, and announcements are already happening as of this writing, there will be retaliation. China will match our tariffs. Other countries will follow suit.

Markets will, understandably, not like the escalating trade war and will be jittery. Expect large down days. Expect large up days. Volatility, will unfortunately, be en vogue.

After that is where it gets tricky. I believe there are three possibilities:

1) The Trump Administration reverses course.
2) The Trump Administration doubles down.
3) The Trump Administration maintains course.

If No. 1 occurs, markets will rally and rally strongly. Perhaps No. 1 comes with a more measured approach to bringing down the trade deficit (we can hope).

If No. 2 occurs, markets will not be happy, and the Trump Administration will feel more pressure from various stakeholders. This may increase the likelihood of No. 1.

If No. 3 occurs, and this is simply our new reality, we will likely see a short-lived market adjustment (and temper tantrum), and then the world will begin to adjust. At a minimum, this will involve increased domestic spending in European countries (as we have already seen in Germany), and a re-shoring of manufacturing back to the United States. But be aware, these changes take time. It has taken 80 years to build to this level of globalization and free trade…it will certainly take time to reverse course. Factories cannot be built overnight, and supply chains do not alter their well-worn paths without a lengthy lead-up in investment and incentives.

At the beginning of the year, I predicted significant bumpiness ahead and, while I would have never guessed we would see such an extreme mandate…bumpiness is clearly afoot.

And yet, we have lived through worse before. In 1987, markets were down a bit over 20% in a single day. In the 2007/2008 crisis, markets lost nearly half their value. And yet, fast forward, and those large sell-offs are hardly a blip in the cumulative growth of equity markets. Capital markets have a remarkable way of utilizing capital for productive purposes…and creating enough incentives to outweigh and outsmart even the most surprising of policy decisions.

Buckle up, folks, we certainly won't be suffering from a lack of items to unpack.

We remain at your service and watching closely.

Daken J. Vanderburg, CFA
Chief Investment Officer
MassMutual Wealth Management

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