This Time is Different

Weekender

August 2, 2025

Genetics is not about fate. It is about opportunity.

J Craig Venter

There are as many atoms in a single molecule of your DNA
as there are stars in the typical galaxy.
We are, each of us, a little universe.

Neil Degrasse Tyson

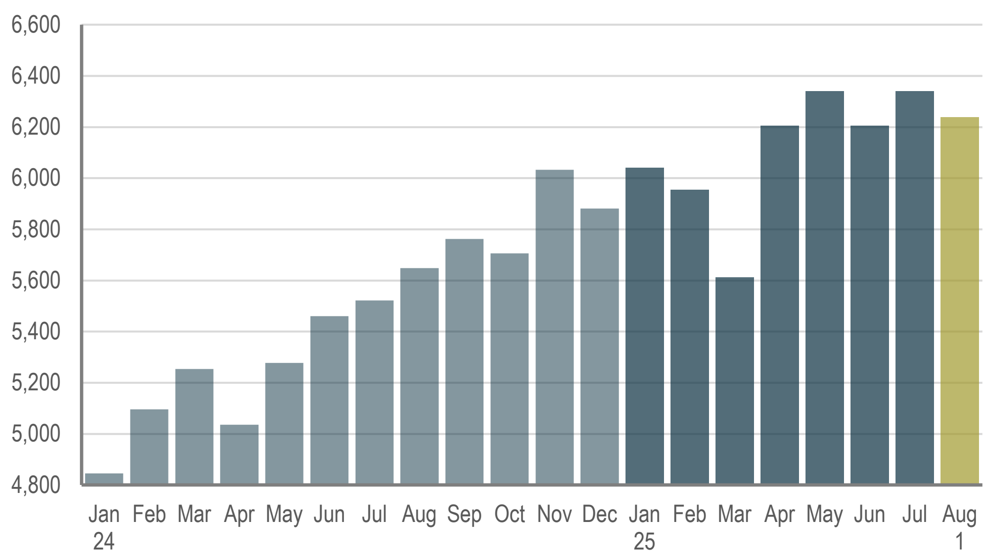
Good morning and welcome to the *Weekender* for Saturday, August 2, 2025. Equity markets, as measured by the Standard and Poor's 500, were down by -2.4% on the week. From the market's pre-tariff peak on February 19 to the tariff angst bottom on April 8, 2025, US equities fell by -18.9%. On April 9, President Trump announced a 90-day stay of tariff execution and advised Americans to buy stocks. From the bottom to the interim peak on July 28, the same markets bounced back by 28.2%. Absent any valid tariff data, this mini bull run was driven by market hallucinations and expectations that the most jarring restructuring of global trade in a century would be benign for both the economy and financial markets.

Economic data from last week suggests reality is poking through the fiction—at least a little.

Be sure to seek qualified investment advice before making investment decisions.

S&P 500 Index Levels

(Source: Bloomberg)



Market Narrative

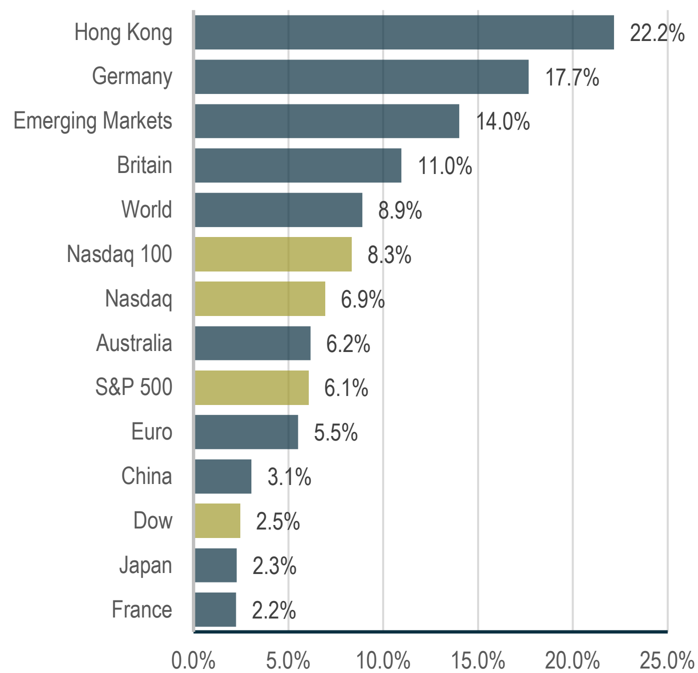
Although we remain fully invested, we believe the data is ripe for misinterpretation. We have been consolidating data, cleaning it from tariff-induced hallucinations, and trying to look forward to market drivers that will emerge in the coming years. We will likely need additional data for at least two months before we can reasonably chart a path forward. We are preparing for several potential scenarios. When we perceive some clarity in the future direction, we will act without delay.

Recent tariff interregnum gains in U.S.-domiciled equities still lag most of the rest of the world. Hong Kong leads, followed by Europe. However, after a dismal start to the year, US equity markets are holding their own.

Looking at valuations, US equity markets remain overvalued compared to historic norms and averages. Despite

Year-to-Date Country Returns

(Source: Bloomberg)



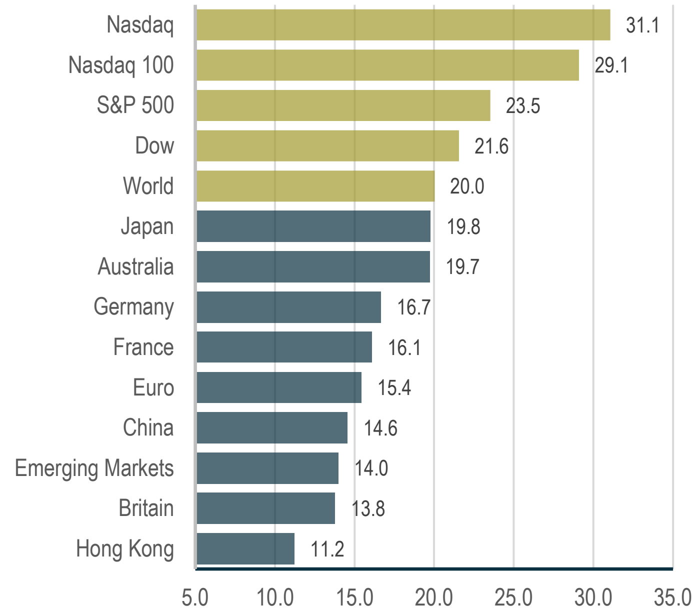
Europe's strong year-to-date performance, most non-US equity markets remain cheaper than America.

No real year-to-date trends stand out when looking at sectors. Industrial stocks, considered to be pro-cyclical, are the best performing, while consumer discretionary stocks, also considered to be pro-cyclical, are logging the poorest returns. We believe US equities are also significantly overvalued compared to the rest of the world.

Economic Narrative

Country PE Ratios

(Source: Bloomberg)



The on-and-off whack-a-mole nature of the Trump administration's tariff strategy has the global economy and financial markets in a state of confusion. Tested economic theories struggle against data releases that conflict with one another. Meanwhile, President Trump dismisses data he dislikes and shoots the messenger. None of this is positive for getting any real clarity in the near term.

We believe it's important to step outside the fog of the tariff environment and cobble together a tentative and conditional narrative for the US economy.

> ***Economic Growth.*** Approximately 67.7% of economic growth comes from consumer spending. The rest comes from investments, government spending, and trade. Tariff policies and expectations have untethered economic incentives and expectations from what is typical. On a headline level, second-quarter economic growth came in at an annualized rate of 3.0%, beating expectations and leading the cognitively careless to declare that tariffs do not impact economic output after all. Unboxing the headline number reveals that when anomalous tariff-related items are eliminated, economic growth was a tepid 1.3%. Much slower than potential.
>
> As we have telegraphed for some time, we believe the US economy is weakening. A narrative not evident in some headline numbers. Prospective tariffs have pushed forward consumer spending, corporate investment, and trade. Advance buying gives the impression that the economy is power-

ing forward in a "damn the torpedoes, full steam ahead" disregard for the risks. We believe that as this preemptive wave recedes, the economy will post much slower growth. If the labor market breaks, we could find ourselves in recession.

Consumption. Consumers are employed and earning, which are the primary determinants of consumption. They are also deeply in debt at increasingly punitive interest rates. Student loans are beginning to bear down on family budgets. Following the summer vacation and frolic season, many consumers experience the sticker shock of looking at their credit card balances while quizzically asking their partners about the unidentifiable charges. Then comes deleveraging. We expect consumers to wade through spending until the holiday season is over and then begin reconciling family budgets.

Labor. The labor market is slowing fast. There are still more job openings than people who are looking for jobs. However, it's becoming increasingly challenging to find a job, and new graduates with limited experience are struggling to connect with a position. Last month, the US economy only added 73,000 jobs. Estimated job gains for the previous month were revised lower than previously announced. Firmly attached workers are much less willing to quit existing positions. Employers are hesitant to lay off workers, but they have already begun cutting contract positions and projects. The US unemployment rate currently sits at 4.2%, which is within the range that most economists consider full employment. We believe a robust labor market is key to economic and corporate profit stability. While we think an economic slowdown is inevitable, financial recessions are always accompanied by a broken labor market. There are no signs that the labor market is experiencing the type of stress that could precipitate a break.

Inflation. Commonly accepted inflation measures at the consumer and producer levels are all showing signs of advancing price pressures. None of the data suggests a price surge on the horizon, but the slow move of inflation toward the 2.0% goal has reversed and is unlikely to turn persistently lower for a year or more. In favor of inflation, crude oil prices are likely to continue a slow march lower as OPEC agrees to increase its output. Pricing on interest rate-sensitive products has also begun to fall. Automobiles, recreational vehicles, and other durable goods are starting to drop in price as rising inventories and high interest rates create incredible buyer demand. We believe the economy can handle inflation between 2.0% and 4.0%.

Interest Rates. On the eve of President Trump's inauguration, the US Government 10-Year bond yields peaked at 4.8%. A general wax and wane of prospective economic prospects has been whipsawing interest rates since the beginning of the year. Last week's tepid economic news sent yields lower in anticipation of a reduction in the Federal Reserve's policy rate during their meeting in September.

Tariff Narrative

During the tariff interregnum from early April to the end of July, market pundits have been aflutter with justification for the market's trek upward. Until last week, investment strategists were in a capitulation mood, declaring that perhaps President Trump was right after all. Tariffs are not inflationary. And, if so, the US economy and corporate earnings may be able to weather higher tariffs with modest effect. This narrative became increasingly dominant after the first tariff deadline fell to a healthy dose of realism. As each succeeding deadline came and went, the acronym TACO, Trump Always Chickens Out, was increasingly likely to be the epitaph for his default foreign policy.

All pundits aside, the issue is simple. Higher tariffs result in higher prices. They are an increase in the final cost of the good being tariffed. What is not simple is where in the value chain the impact of the tariff will be borne. If the exporter and/or importer bears the weight of the tariff, their profit margins will be compressed, profits will shrink, and the stock price will fall. Consumers may also bear all or part of the tariff through price increases, which will result in a reduction in spending on both tariffed and non-tariffed goods and services.

Since TACO Wednesday on April 2, economists, strategists, and analysts have been carefully watching data in an attempt to gauge the tangible impact of Trump's tariffs. It has not been nearly as difficult as predicted, stage right all the justifications for markets rising. However, a few things are worth considering. Trump's Tariff saber-rattling began in early February, on the heels of his inauguration. As a precaution, many companies dramatically increased purchases of potentially tariffed goods in advance. Pre-purchased goods were sufficient to pre-build inventories, which in some cases will not be used up until early 2026.

Our view is that the "doo doo," a technical financial term, from tariffs is delayed in transit. The full impact will not occur until the end of the year. We believe it's essential to be adept in making any portfolio changes. We have been purposely positioned in defensive names and will continue to do so. However, we anticipate that going into the end of the year, when we typically rebalance, our risk profile will come down.

This Time is Different

By most seasoned investors and market voyeurs, financial markets are deemed to be mean-reverting. When valuations deviate too far from average, an average return can be expected, although sometimes it takes far longer than predicted. Even so, at reasonably regular intervals, market dynamics are influenced by fads, trends, and changes that provoke some to declare that a new era has broken and the reversion ended. From 2000 – 01, many acolytes went so far as to declare that the need for profit and cash flow was old-fashioned. Eyeballs and page views were all that mattered. However, for anyone with staying power, the steady hand of sages and prophets steadied the market in its reversion.

When someone promotes a trend or idea so revolutionary that "this time is different" investors over forty roll their eyes and hold on to their wallet. But something is different. We are not talking about artificial intelligence, which, without question, will be life-changing. Instead, we are watching a structural change in financial markets themselves.

The internet technical revolutions spawned the use of equity as a means of attracting and compensating talented employees. It also accelerated share repurchases as a form of compensation for shareholders.
From the year 2000 until 2011, the total shares outstanding for members of the S&P 500 rose dramatically as firms increased equity-linked compensation and equity issuance to fund technology investments. However, since 2011, a low-interest-rate environment has made debt a more attractive capital source. At the same time, technology companies were generating mountains of cash, permitting them to dramatically increase cash compensation and tighten equity grants to a smaller pool of influential employees. The combination of low interest rates and strong free cash flow also permitted stock buybacks to reach consecutive records every year.

Passive investing reached its tipping point in 2000, which dramatically increased the amount of investment capital coming into the markets and buying securities without a sense for price, value, or fundamental discrimination.

The primary influences described above catalyzed a phenomenon where the number of shares outstanding and available for purchase began a precipitous decline while the investment capital looking for shares to buy rose significantly.

The blue line represents the number of shares outstanding in the S&P 500, while the gold line rep-

S&P 500 Shares Outstanding (Blue) and AUM of SPDR (Gold)
(Source: Bloomberg)

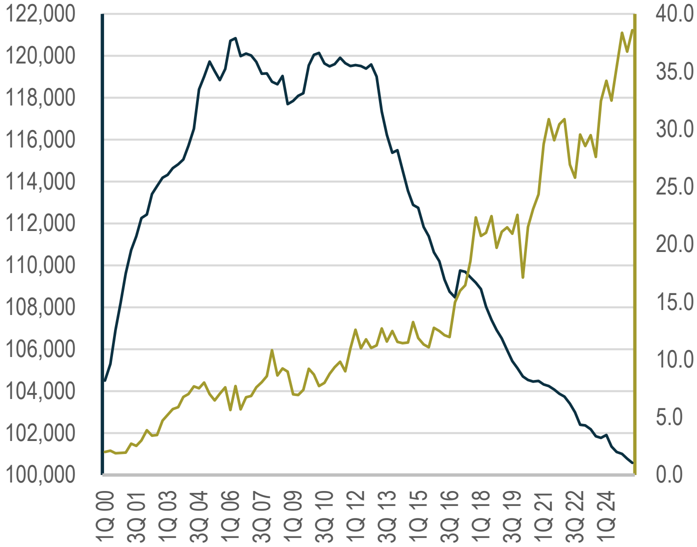
resents the assets under management in the primary exchange-traded fund that follows the S&P 500.

Similar results are exhibited for the Dow Jones Industrial Average. The blue line represents the number of shares outstanding in the Dow, while the gold line represents the assets under management in the primary exchange-traded fund that follows the Dow.

The point? Fewer shares and more money have enabled valuations that are perpetually higher than the historical average. However, in a post-pandemic world, interest rates are rising, making debt less attractive. At the tail end of the baby boom generation, boomers will soon begin living off their investments

S&P 500 Shares Outstanding (Blue) and AUM of DIA (Gold)

(Source: Bloomberg)



instead of building their corpus. The result will be less upward pressure on valuations over time.

Conclusion

That's it for this *Weekender*. Have a wonderful week.

Disclosure Statement

Index performance does not reflect the deduction of any fees and expenses, and if deducted, performance would be reduced. Indexes are unmanaged and investors cannot invest directly in an index. Past performance does not guarantee future results. Investing involves risk, including loss of principal.

The statements provided herein are based solely on the opinions of the author(s) and are being provided for general information purposes only. The information provided or any opinion expressed does not constitute an offer or a solicitation to buy or sell any securities or other financial instruments. Opinions expressed are subject to change without notice and are not intended as investment advice or to predict future performance. Economic forecasts set forth may not develop as predicted and there can be no guarantee that strategies promoted will be successful. The foregoing information has been obtained from sources considered to be reliable, but we do not guarantee it is accurate or complete. Consult your financial professional before making any investment decision.