# The Oak Financial Times

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Written and Published by Oak's Investment Team

**"Good times never seemed so good**
**I've been inclined to believe they never would"**

- Neil Diamond, Sweet Caroline

There has been a growing chorus on Wall Street lately that this time is different. In studying financial history the catalysts, we were taught that cause recessions have not yet materialized. The combination of fiscal and monetary policy has expanded the Fed's balance sheet from one trillion dollars to nine trillion dollars over the past fifteen years. This has most likely caused investors to take on more risks, spend unabashedly, and become extremely complacent. We have lived through multiple decades where the public has become conditioned to believe that every time markets stumble the central bank, or government will have their backs. So, we ask again, is this time different?

Last year the Federal Reserve lowered interest rates 100 basis points (1%) between September and December and instead of declining long-term interest rates rose. Markets are starting to realize that central banks have run out of tools. It seems obvious at this point that the Fed can no longer raise interest rates as it will kill both the economy as well as the banking system and they are not inclined to cut rates currently for fear that inflation will accelerate once again.

Jay Powell must also keep one eye peeled on China as deflation has set in with their interest rates falling to 1% late last year. This is important as China kept world economies afloat during the market crash in 2008 with a then strong economy. Today they cannot act as a relief valve for the world as theirs is in disarray.

There is a huge debt load around the world with currently no solutions on the horizon on how to address it. Additionally, a tariff war was unleashed with an outcome unknown. The period of low interest rates following the 2008 Global Financial Crisis and the 2020 pandemic were stimulants that aided the explosion of debt. Our aging population, large defense spending, and increasing interest costs will all

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contribute to keeping debt at elevated levels.

A case can be made for all scenarios leading to inflation, or deflation, or stagflation. The two main drivers of inflation are the twin deficits and a shortage of workers due to declining population coupled with expulsion of immigrants. Deflation could occur as the advent of artificial intelligence and with the new mantra of drill baby drill lowering the cost of goods and services we utilize daily. Stagflation, known as a combination of inflation plus low growth, could emerge due to the implementation of tariffs increasing prices and the consumer pulling back.

Scott Bessent, the Treasury Secretary nominated by President Trump, has stated that his plan is to cut the national debt in half. Mr. Bessent has advocated that the ten-year Treasury yield is the key factor to focus on as it determines both company and individual borrowing costs. To do this, he will need to increase gross domestic product to three percent and at the same time bring inflation down to three percent. We are hopeful that he will be able to accomplish this, but our confidence level is currently very low.

It is not only the budget deficit that is an issue, but trade relations are also a large concern. Trade imbalances can arguable be traced back to 2001 when China was allowed to join the World Trade Organization. It was thought at the time this would allow U.S. domestic corporations to ship their products to an additional 1.3 billion new customers. It allowed U.S. corporations to lower manufacturing costs by using China for cheaper labor to enhance their company earnings.

Through the years this has caused the Chinese to build up huge surpluses, and since their currency is linked to the U.S. dollar, they accumulated a large stockpile of our currency. The Chinese then took those surplus dollars and bought stocks and bonds in the U.S. making it an equitable arrangement for all parties. The Trump administration has been clear that they wish to either reduce or eliminate their trade deficit with China but anyone who believes that Xi Jinping will bow to Trump is probably misguided. Past good times may take a long time to look so good again.

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**WTF?!?**

It seems only fitting that a year beginning with a **W**ednesday, **T**hursday, **F**riday sequence, would yield so many head scratching moments in only four months. And why not start this newsletter off with a little tongue and cheek word play before digging into the weeds.

On April 2, 2025, President Donald Trump introduced a series of sweeping tariffs aimed at recalibrating the United States' trade relationships with several major global players, including China, the European Union, Mexico, and Canada. The tariffs, covering over $900 billion in goods, are part of Trump's broader strategy to reduce the U.S. trade deficit, stimulate domestic manufacturing, and protect U.S. jobs.

These tariffs are among the most aggressive trade policies since the global trade wars of the 1930's. Their implications stretch far beyond U.S. borders, affecting global markets and the everyday economy. After Trump's announcement of the tariffs, global markets experienced extreme volatility, and the outcomes are still being unpacked.

Trump's decision to implement these tariffs was based on his administration's longstanding focus on "America First" policies. The tariffs were calculated with the goal of making U.S. products more competitive relative to cheaper imports, especially from countries like China, which Trump accused of unfair trade practices, such as currency manipulation and intellectual property theft. The U.S. aimed to force trading partners into renegotiating existing trade agreements that Trump argued were unfavorable to America.

Key sectors targeted by these tariffs include electronics, steel, and agriculture, with the expectation that companies would shift production back to the U.S. to take advantage of tariff protection. In this context, the Trump administration believed that tariffs would push American businesses to increase investment in domestic manufacturing, thus generating new jobs and promoting self-sufficiency.

Trump's administration laid out their plan for implementation; it began in phases, with the first round focusing on Chinese imports, followed by European and Mexican goods. The government stated that there would be periodic reviews of the impact on various industries and adjustments made accordingly. We have seen a few rewrites to the reciprocal tariffs already and their effects are all over the place.

Trump believed that the tariffs would push foreign governments to comply with U.S. demands for better trade deals. It is still TBD if it will work and if other countries will come to the negotiating table.

Internationally, these tariffs have been met with widespread criticism. Many economists, money managers and Congress members of both political parties argue that the tariffs undermine global trade and could potentially lead to a global recession. Heavy financial hitters like Jamie Dimon, Ray Dalio, Stan Druckenmiller and Elon Musk have expressed concerns that such measures could spark broader economic instability. Key trading partners like China and the EU have threatened and enacted retaliation, deepening the divide between the U.S. and its allies.

Politically, Trump's tariffs have sparked debate within the U.S. itself. While some Republicans support the measures, believing they align with Trump's populist agenda and will benefit American workers, many economists and Democratic leaders have warned about the long-term damage to the economy. Former Treasury Secretary Lawrence Summers predicted that the tariffs could lead to significant job losses and an increase in consumer prices, ultimately hurting average American households.

This political move represents a bold and controversial strategy to reshape global trade and restore American manufacturing. While the tariffs offer some potential benefits, such as protecting domestic industries and reducing the trade deficit, they also come with significant drawbacks, including higher consumer prices, global economic disruptions, and strained international relations. As the world watches closely, the full impact of these tariffs will unfold in the months and years to come.

As we continue to monitor these developments, we remain committed to navigating the evolving economic landscape to the best of our ability.  We hope WTF will only be reflective on how this year's days started and will not be how the year is remembered, but we will be prepared if it is.

**CONCLUSIONS**

1. In addition to the tariff wars, another big concern is that the Federal Reserve prematurely lowers short term interest rates and inflation takes off again.

2. If DOGE is successful in cutting a minimum of $500 billion in the Federal budget, we should expect the unemployment rate to continue to rise.

3. Both fiscal and monetary policy that have inflated equities in the past few years are soon to reverse.

4. DeepSeek, the Chinese artificial intelligence company who recently made headlines is a big deal. Other corporations in the AI space that have spent billions are now learning there's a better, cheaper and faster competitor waiting to eat their lunch and make those previous investments seem wasteful.

5. Focusing on an investments' correlation to the strength/weakness of the U.S. dollar needs to be on the forefront of your mind.