DIVIDENDCAFE | PODCAST TRANSCRIPTION

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Hello and welcome to the Dividend Cafe. I am your host, David Bahnsen, managing partner at the Bahnsen Group and back in our Newport Beach studio where I have actually not been for about six weeks.

And it is nice to be back here at this home base. What being back has not done is rally markets. We're recording right now on a Friday morning where markets are in sell off mode. Around tariff and price volatility, but they started the week off in a big rally, and so it may end up ending as a week reasonably close to where it started, but that day-to-day uncertainty, volatility continues to be a big story in markets, not really down a ton from where the highs were about two months ago when a lot of this drama started.

But nevertheless down and not really recovering. And then a lot of question as to where we're gonna go from here. And that's the subject of today's Dividend Cafe is trying to get a feel for where I believe we are in the context of going into next week, because the administration chose to set this up.

One point, referring to April 2nd, which is this coming Wednesday. As liberation day and there is a line drawn that a lot of tariff announcements are coming and markets have begun pricing that in the issue though is that the line is really nothing more than April 2nd, a day that supposedly you're gonna know more along the way what it is that we're supposed to be finding out.

About reciprocal tariffs or about the vat or about dealing with non tariff barriers to trade in certain countries, certain products, certain sectors. Some announcements came out already. Some we don't know what we're gonna hear, what we are expecting to hear has changed. So there's a significant amount of chaos and I think there are market actors.

That are expecting this coming Wednesday, April 2nd to be a point where even if it's a lot of bad news, at least we're gonna find out what's going on this week. And I happen to disagree with that viewpoint. I'm not really totally sure that we're gonna have much clarity this week as to what's going on, but we'll find out

first of all, just to understand. In terms of some economic vulnerability. I'm gonna put this out there first and we're gonna come back to it in a moment. Copper this week, a record all time high. Perhaps one the most important industrial metal, very vital to industrial production, construction, et cetera.

Steel prices are up 30% since the inauguration. Lumber prices are up 18% since the inauguration. I wanna hold those things in place for a moment. Here's a quote from President Trump. This week. I'll probably be more lenient than reciprocal regarding tariffs, because if I was reciprocal, that would be very tough for people.

It had been announced I was getting popups from Bloomberg and Wall Street Journal on Sunday. The market rally earlier this week was Monday. He said that on Tuesday. But that underlying narrative being, it's not gonna be as bad as you may have thought. He additionally said, I know there are some exceptions coming.

It's an ongoing discussion, but not too many exceptions. Not too many and so I think it's important to understand where some of the market hope was is okay, we're back in the same mode where they're barking loud, but they're not gonna bite as hard. And that was the story of 2018. It was the story back in January, February, some of the Mexico, Canada stuff.

And these things have been on again, off again, and this idea of reciprocal tariffs. The European Union has said they're expecting a 20% tariff implemented across the board. There's been a lot of other talk that the commerce department is allegedly trying to decipher what the tariff levels are with individual countries.

And then there's question as to whether or not they're including in that calculation, the impact of the vat, the value added tax, the impact of other barriers. I put a chart in Dividend Cafe.com this week that shows the very large difference across different countries, and what portion of this level of cost is from a straight tariff versus other barriers.

The point being it's all over the map. I don't know where the European Union is coming up with the 20% expected tariff. It very well could be the case, , if they were to just do a straight reciprocal, the actual numbers, as to what it would represent, you would be dealing with $160 billion of additional taxes if a reciprocal vat were imposed.

But if there are reciprocal tariffs that are equal to the current level. Then you're talking about a grand total of 1.5% above the current level, so the 20% being done across all 27 European Union countries. That would mean they're incorporating that and the administration's not said they're gonna do that.

It doesn't mean they're not. I just don't know, and I don't believe anyone else knows. And then the issue I'm coming to you today to say is, I don't think you're gonna know April 2nd. That's not to say they won't make an announcement. I think they can make an announcement April 2nd and change it April 3rd, or make an announcement on April 2nd and not change it April 3rd, but have the enforcement on April 4th be totally different or have some company or country make a big announcement and on April 8th, and then get a big carve out from it.

As proof, which, by the way, this was my thesis after my time at Treasury last week. And the way I wanted to unpack this is an investment narrative about ongoing uncertainty, not pricing in the certain bad news we get next week, and not making a prediction of getting certain good news, but more making a prediction that we're not really gonna get this thing resolved next week, that April 2nd is more of a political line, but not a market or investment or an economic line.

But then after I began writing Div Cafe this week. We got validation of the thesis in the form of President Trump's pressor on Wednesday night, announcing the auto tariffs. They leaked to the Wall Street Journal in the middle of the afternoon, Wednesday. That auto parts were gonna be exempted. Then he made the announcement Wednesday night and auto parts were not exempted and automobile imports and auto part imports, they didn't wait until April 2nd.

They put that out ahead of time. So there is some degree, you always get these theories that people saying they're playing four dimensional chess. They're not.

That doesn't mean that everything is bad. It doesn't mean everything's good, but it is not all intentional and strategic. There is a certain chaotic atmosphere that I have no reason to believe goes away in a few days.

So again what we're talking about here in terms of market actors from the vantage point of the clients of the Bonds group and those of you who are our investors, is, I'll make a quick point on reciprocity. If we were only doing reciprocal tariffs and not factoring in the vat cost that Europeans charge to Europeans, you would barely be getting much increase.

If they're just gonna do a flat level across all, then it's a much higher cost than people realize. But then it's gonna immediately, I think, start begging for carve outs and exceptions. If we're trying to get to a point of what they call fairness, I wanna point out. That the tariffs that are being imposed by certain countries are being paid by their country's importers.

And what we are suggesting is we're gonna punish Germany by charging our country's importers, our country's consumers for what Germany's doing. So I don't believe that there's going to be a lot of stickiness to the substance of the argument, but if we believe it's as President Trump alluded earlier the week.

Not gonna be as severe then maybe markets priced in more than is coming. And yet the news of a 25% tariff on all auto imports was announced Wednesday night. Now markets didn't care Thursday at all. And the, in fact, Volkswagen was up and a couple European automakers were down a little Volkswagen was up and there and the US automakers were down the most.

And so I, I think that what we're dealing with is a broad issue of cost that will come to Americans and a complexity. Let's use the auto issue as an example. US automakers import a lot of parts, so there's a cost to them. Obviously a lot of foreign automakers. Exporting to us. And so they're gonna be subject to this higher cost as it gets imported into America.

So who do you think stands to benefit the most if this is hurting? Both foreign and domestic. Automakers used cars and so this is not new production. This is a benefit to a secondary market if that were to play out that way. I'm not sure that's really the most visible effect benefit that the president's going to, but you know, when I use that term visible effect, that kind of tees up the biggest point I wanna make when those that are hearing it at a high level.

Are saying, okay, look David, there's uncertainty and we've seen the stock market get a little volatile here, but you yourself have said it hasn't been that bad and I stand by that a hundred percent. It's been nothing severe historically whatsoever at this point. Do I believe that that's the real cost is just a little volatility in market?

No. I believe the cost is invisible effects that, that we effectively. Say, oh, we think that visibly we're gonna help American manufacturing jobs. And I don't agree with that assessment, but if I did, we are missing the impact. American Services, jobs, we have 17 million people in this country employed in hospitality, travel, leisure.

You get significant decrease in tourism from Canada, for example. There is a cost there, and you can say, I don't care. And you can say, I don't think it'd be that bad, but you can't say there's not a cost. That's where these different trade offs are. And I think that the economic impact right now has been categorized around a couple different lanes.

One is the real cost that's visible lumber prices and copper prices and steel prices that I brought up earlier. Those visible and short term cost. A problem. Now some will say there's gonna be visible short term benefits and maybe there will be, and maybe you just think those things offset. I don't happen to agree, but there is on the table right now, the visible short term cost and downside.

But then I think beyond that, the issue we're dealing with is fears of economic slowdown. And this is where the idea that a lot of the tariff stuff doesn't end up happening, or you get better deals, it may very well not matter because if you along the way to getting to the point that you're pump faking that you generate enough uncertainty that you generate enough inactivity, you may very well get a self fulfilling prophecy.

That could tip the economy this summer into recession. Now, this week we got a very, very low consumer confidence print. It was a 12 year low, and ironically, even for someone who's very much on this theme of what the impact is gonna be from uncertainty caused outta tariffs, I think that's nothing burger, because I don't believe Americans.

Have poor sentiment about spending. They famously say, we have no confidence. We have poor sentiment. Excuse me, get outta my way. I'm going to the mall. This is the almost exclusive pattern of Americans is to either say they feel good about spending a lot or to say they feel bad about spending a lot, but never to say that they're not spending a lot.

I am far more focused as a supply sider in the impact of production. And this week we also got a read that non-defense capital goods orders fell 0.3% in February in one month. They were expecting a 0.2% gain, so you had a half a percent switch in one month in expectation, and orders had been up 0.9% in January.

Now I am well aware of the fact that one month is not enough. To call a pattern, call a trend. It's the beginning of a data series and we'll see where it goes, but it's a stark data warning of capital goods orders dropping like that in one month, right? In concert with this elevated tariff and trade talk.

But what was more interesting to me, and I edited it down, trimmed it down. So I think about a dozen bullet points@dividendcafe.com. I'm not gonna read all of them verbatim right now here on the podcast, but they are made available just as they are from the Dallas Fed Survey that came out this week.

And a lot of the sector representation. Dallas Fed is in ENP, the expiration production oil and gas sector. This is Red State region. This is very Trump administration friendly. Re sector both geographically and the professional business sector, and the comments are overwhelmingly negative about the uncertainty, and there were plenty of comments about uncertainty about commodity prices.

And just reinforcing that we're sorry we're not drilling at $50 oil. If you get down to 50, we're out. But, 66 is not 50, but it's also not 76. And so a lot of that talk is legitimate commodity supply demand, back and forth concerns that this is what they do for a living in the oil and gas sector.

And yet there were other comments that were much more noteworthy and more or less systemic about the uncertainty caused by the tariffs, the uncertainty. Commodity markets tariff policy making impossible for us to predict. We don't have a clear goal. We want more stability. Administration's tariffs are increasing the cost of our casing and tubing by 25%.

Even though inventory costs our pipe brokers less. Tubular manufacturers immediately raise their prices to reflect the tariffs on steel. I've never felt more uncertainty about our business in my entire 40 plus year career. Steel prices, overall labor, joint costs are up relative to the price of oil.

Geopolitical and risk economic uncertainty. Cloud our picture looking forward. Unstable capital markets the steel has already purchased. Tariffs will impact our 2026 investment decisions. Washington tariff policy, injecting uncertainty in supply chain. These are people I suspect, voted for President Trump.

I can't prove it. I don't know that all of them did, but yeah, I don't think there's a lot of oil and gas executives in Texas. We're not Trump voters, and this is what they're saying about the uncertainty here. So I'm not making political comments and I promise you they weren't making political comments.

I think that we are dealing with a certain elevated uncertainty that is problematic for the economy, no matter what is going to happen with tariffs and no matter what one thing should happen. This is where I want to end things today. What is going to happen next week? Should not surprise you to know that I do not know and that neither do you and neither does anybody else.

And yet my additional point is I don't think anyone in the White House does either, quite possibly including the person who's in charge of it. There is a lack of clarity and. I would argue that the concern we're gonna get to a place of a permanent elevated tariff environment, a sort of imposed cost, an imposed trade barrier that is coming.

I would argue it is all at once, not impossible. It is not my base case, but it is very close to a base case. It's on the table. It is what the administration's threatening and it is what some of the administration spokespeople are publicly advocating for new sheriff in town, new environment, new tariffs, that we're gonna try to create a structural reordering of the way trade flows work and doing so be out of a belief that they wanna bring the trade deficit down.

I believe that the trade deficit will not go down even if they succeed in decreasing imports. I don't know why we'd want to decrease imports, but let's just pretend we think that's a good thing and let's pretend we think it's gonna help American jobs, which I do not think it will. However, net net, however.

It will decrease American exports too. So if one side of the pool is going out, the other side of the pool going out, you're not doing anything to lift the pool and you're not changing the direction of it. And a trade deficits of byproduct of imports and exports. So if they're both going down in concert, all you've done is bring down total trade, not the gap between imports and exports, which is what the trade deficit is.

I think President Trump would like a headline victory out of this. I think he's determined to get one. If one asked me to bet not with client money, not with my own money, not with investment capital that is attached to long-term goals, but just place a wage or will he end up claiming some sort of headline victory out of this in 2025 or 26 or some point in this administration, I would bet he's going to.

The issue is will that headline victory be, I got the trade deficit down, I'm skeptical. Will it be we avoided recession? If they do go forward with all this, I'm very skeptical. The issue is gonna be what are the catalyst that caused the president to potentially reverse? And a lot of people on my side of this issue think that that is gone.

It's off the table that they're determined to go fully forward. And maybe they are. But I think a win for America matters to the pathology of the country, at least a perceived win, a cosmetic win. And there's another thing he said this week that you ought to have in your calculus right now, the auto tariff thing, the threat of reciprocity, what the EU said, what they said on Monday, what markets have done.

Then you hear the president say, I could knock down the tariffs on China a couple percent if they let us divest TikTok some social media app for 15 year olds. And this vitally important thing to even out global trade to right the wrongs of the WTO for 25 years. And yet that could be just cast aside if they let us have our dancing teenager app back or something.

I don't know that any of this sounds like the administration is that serious about making it permanent. I don't know that they won't. I do know they're threatening. All I'm saying is it is not true that somebody can look at the facts on the table and say, we have total clarity as to what's going on.

Then the concern, which I have had at points over the last six weeks, that all of this talk of trade and tariff. Which is certainly capturing media oxygen and market oxygen is also indicative of behind the scenes deprioritization of tax reform. And I did come away from my time in Washington last week, very convinced that's not the case in treasury.

There are voices on President Trump's shoulder. A lot of them are from Trump 1.0 that are adamantly reinforcing the supply side priorities that need to happen. Much of the messaging I'm hearing from Secretary Bestin Treasury and from Kevin Hassett, national Economic Council. Even if they say a couple flirty things, fsy things about tariffs here and there, they most certainly are reinforcing that there needs to be a supply shock, upside out of tax reform permanence of tax, of prior Trump tax cuts, deregulation and energy independence, and that policy portfolio.

Hasn't changed there, and I don't really believe it's changed with the president of the United States either. But I do understand that the public messaging makes it look like it's been deprioritized. I am all at once a little less concerned that it's been deprioritized as an agenda, but I am more concerned about the just d challenge and complexity and difficulty of getting it done.

There is a really tight rope to walk here and getting one big, beautiful bill done as the president said by May can happen and would be very offsetting to a lot of the economic issues from the tariff side. But it is not a foregone conclusion that it will. And when people say, is it 50 50, 40 60, 60 40, I can't do all that.

It's somewhere in between there. Somewhere between 30 70 and 70 30. Okay. So it isn't a very, very high odds and it isn't a very low odds, but that leaves a lot of bandwidth in between. Okay. Two things I wanna say to you. On the tax reform side, that is barely discussed right now because of auto parts and TikTok and tariffs and all the whatever.

A, a policy baseline being used if there is some announcement made that they've reached an arrangement and the Senate parliamentarian agrees that they will be able to attach a budget reconciliation based on this year's actual policy and not where those sunset and tax cuts were supposed to go. That's worth about two and a half trillion dollars of additional bandwidth in where they go with a tax bill.

Policy baseline is a massive undetermined variable, still looming. Number two, without getting into a lot of details and a lot of both meetings out in New York this last week and DC week before, but Senator Mike Crapo from the great state of Idaho is a key figure here. When you look at the big players, Jason Smith at house ways and means.

Secretary Bessent, Kevin Hassett at NEC. Obviously President Trump, obviously Speaker Mike Johnson, obviously Senate Majority leader John Thune. There's a lot of political actors and policy makers that have to drive what's gonna happen or not happen with tax reform. But Mike Crapo at the Senate Finances one behind the scenes driving and I am convinced doing some real four dimensional chess that a lot of people don't know about that I think may pull this across the finish line.

So that story I have to keep watching and monitoring and allowing it to impact the way we're viewing what could happen with the economy this year, just as much as whatever this April 2nd melodrama is supposed to be. So I'm gonna leave it there. We're in for an interesting week ahead. Markets may not have priced in all downside events.

Markets may not have priced in all upside events. That uncertainty persist. I continue to believe there is a Trump put in the market. It's just that I think that strike prices as to where a reversal would come. If markets got bad enough, is much lower than it is now. And if that were to happen, it may very well be fine for risk asset investors, but not for the economy.

I think it would probably come to eight. At that point have tipped the economy into a recession. If you were to get into a real 20% down from peak bear market there are others who say, oh, the Trump puts down even then at 20%. Even in a bear market, the president's gonna go forward all the way. I don't agree with that.

At some point, markets are not gonna get a cohesive, coherent trade policy. This might be the most important thing I say to you today. Probably a more likely scenario is not markets getting cohesive, clear trade, but accepting that they're not gonna get it. Right now markets are still having to respond to the lack of clarity to the incoherence.

But at this point, it's impossible to predict exactly where all this will go. And I will tell you that it's a wonderful thing. That you don't have to there are moving parts upside risk with tax reform, downside risk with tariff upside risk with reversal of tariff. Uncertainty that is up and down about the both exceptions that could come from tariffs.

The not as bad as expected Tariffs, the worst than expected tariffs. All of that's on the table at once. And if you believe that there's ever been a period where there was an upside and downside uncertainty in markets, you're wrong. It's always been there. This is public. This is vocal. I'm talking about every darn week and I'm sick of talking about it, but it's my job.

And I want you to be informed about the way we're thinking about it. But do but anyone who believes I'm supposed to lay a bunch of additional risk on, 'cause this is all gonna boost us a bunch over the next six months. I think it's crazy. And anyone who thinks I need take all the risk off, that was appropriately priced into my portfolio.

That is my portfolio being appropriately constructed around expectations of certain levels of downside volatility, and that somehow this is changing all that. They're very wrong. Portfolios have to have been designed to withstand this, but this is what, this is upside, downside uncertainty that I don't think is going anywhere.

April 2nd, April 3rd, next week. That's where we are in the ongoing saga. Please reach out with any questions you have questions@themonsongroup.com. You are very welcome to email me and tell me that I'm being too nice to the president or I'm being too mean to the president. I'm gonna continue telling you this as long as I keep getting a note every hour from someone saying I have Trump derangement syndrome, which is an absurd accusation, and someone else telling me that I'm all in on MAGA, which is an absurd accusation.

All I'm gonna do is just. Delete and assume I'm doing my job, but that's literally how severe some of these notes are. I'm getting that they're this severe this way and this severe that way, and they can't both be true. I'm doing my best to call balls and strikes on what's happening in the economy. There are things I disagree with, what the president's doing, there's things I agree with, and there's things I don't know what they're gonna end up doing.

My point to you is I don't think they know what they're gonna end up doing. That doesn't make me one side or the other on this. I'm trying to analyze it in the vantage point of being an objective economic thinker on behalf of my clients whose portfolios we manage. To that end, we work. Thank you for watching, listening and reading the Dividend Cafe.