Commerce Trust Market Brief with Scott Colbert

January 27, 2025 – Trump Presidency and Potential Impacts to the Economy and the Markets

Scott Colbert: Good morning. It's Monday, January 27th and the markets are open. And so far this year we've had basically a continuation of where we ended last year in terms of the market result.

The S&P 500 (Index) is up a whopping 3.8% already so far year-to-date. Mid-cap (capitalization) stocks are slightly outperforming the larger stocks. A little bit of broadening in the market there, up 4.85% (as measured by the Russell Midcap Index). Smaller cap stocks though when you get really down to the smaller companies still are underperforming the S&P 500 but still up 3.51% year-to-date (as measured by the Russell 2000 Index). International stocks (as measured by the MSCI EAFE Index) are actually outperforming the S&P 500 in a bit of a reversal, up 4.42%. Kind of on a quiet fashion, international stock markets, many of them, have hit record levels, including the British stock market, the French stock market, and German stock market. Emerging markets (as measured by the MSCI Emerging Market Index) are up, but not very much so far this year. And bonds have been the big disappointment.

With Trump's election, the largely pro-growth strategies, possibly some more inflationary pressure, interest rates have risen so far year to date and the total return of the bond market has been effectively zero. Investment grade bonds have returned about nine basis points so far this year, and municipal bonds are just barely negative.

Now, we just mentioned that mid-cap stocks are actually outperforming the S&P 500, a bit of broadening to the market. But when you take some time and look back, when the market really decided that the Federal Reserve was going to cut rates in mid-July, large-cap stocks have still outperformed. The S&P 500 has outperformed by about 2.5% its equally weighted index.

So we still have yet to see very much of this market broadening. We are optimistic that it should, given likely policies that result in more mergers and acquisitions, that ought to be good for smaller companies, as well as a domestic focus that the administration seems to have that also ought to be favorable to local domestically oriented companies, which tend to be smaller companies in general.

Clearly though, the market is focused on our new administration. We'd like to focus on four key areas: taxes, tariffs, immigration, and policy. With regards to taxes, is the extension of Trump's original Tax Cuts and Job(s) Act. But to get that extended, he's (President Trump) likely to offer some accommodation to the Democratic side, which might include higher SALT (State and Local Tax) tax deductions. And then finally, helping corporate taxes fall, particularly for those companies that are focused here in the United States.

In terms of tariffs, we still don't know where this is going to lead, but we have to recognize there's three key drivers. Number one is simply as a negotiating tool having leverage over other countries, for example, less immigration and a stronger border. He (President Trump) wants to focus on unfair trade practices. And then finally, he (President Trump) would like to raise some revenue, although I don't think the revenue raised is going to be nearly enough to put a dent in the deficit.

With regard to immigration, there are three key focuses. Number one would be border security. Number two would be potential deportation of unlawful immigrants currently in the country. And then number three is how many H-1B visas are likely to be issued.

With regard to policy, there are basically five key areas: a focus on energy independence, AI (artificial intelligence) initiatives, a positive backdrop for crypto and cryptocurrency, less regulation in general, and then perhaps greater government efficiency with regard to the DOGE committee (Department of Government Efficiency).

The impact of all these policies with regard to the economy is likely to be what? Higher growth, we've upped our estimates for GDP (Gross Domestic Product). Potentially higher inflation because of the tariffs and the faster growth. Employment growth is likely to be faster. The unemployment rate is likely to remain steady. Recall that it had been rising from 3.4% to 4.2% under the previous administration. But if we do have faster growth, this should put a lid on rising unemployment. Unfortunately, the deficit is likely to be larger, particularly with the extension of the tax cuts. Tariffs aren't likely to offset the costs involved with reducing taxes in general. And then, we are faced with a slightly higher interest rate environment than we likely would have. Note that the 10-Year Treasury is already up about 30 or 40 basis points from Election Day through mid-January.

And we're still focused, of course, on what the top-down risks are to the market. In terms of magnitude, we know it's still an expensive market and a narrow market. We do expect some broadening, and we hope to see some market leadership rotation. We certainly have a deficit. And that deficit is getting more and more attention, and it needs to be addressed.

We've always got the ongoing threat with regard to China, particularly in the China Sea and Taiwan. Now we've got the new possibility of a tariff war, which we haven't seen in quite some time. All of these new policies are bringing about some inflationary pressures that hadn't been expected. And then finally, most recently, we've seen a small startup in China called DeepSeek produce an AI-like, GPT (generative pre-trained transformer) chatbot that seems to do what our AI systems do over here, but much less expensively and more efficiently.

We'll be back in several weeks to discuss new administrative policies and how they're impacting the financial markets.