Donaldson
CAPITAL MANAGEMENT

The Outlook
DCM Market Brief

Choppy Waters

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Since the tariff announcement on April 2, markets have experienced significant volatility. The tariffs were much higher than expected, which caught investors off guard. This led to intense buying and selling as markets grappled with fast-moving headlines.

After the announcement, tariffs increased for some countries and were delayed for others. Overall, tariff levels are considerably higher than before. At one point, the S&P 500 fell by over 20% from its recent high, entering bear market territory. However, it has since recovered and is now about 12% below its all-time high. The market's future trajectory remains uncertain and largely depends on how policymakers react in the coming weeks and months.

The scale of the tariffs sent shockwaves through financial markets. In total, the new measures amount to over $620 billion—about 2% of the U.S. economy—making it possibly the largest tax increase in modern history. Economists now think a recession is more likely and have increased their inflation forecasts, causing more market turmoil.

However, the sharp rise in Treasury bond yields ultimately forced the administration to recalibrate. Concerned about the rising cost of debt service, the focus shifted to targeting China specifically, while some tariffs on other countries were delayed by at least 90 days. While this adjustment did not significantly alter the overall dollar amount of tariffs, markets welcomed the change in tone and direction, prompting a relief rally.

This remains a fluid and fast-changing situation. Higher tariffs will likely persist in some form. The long-term effects are unknown, but consumers are expected to face higher prices in the short term, and the risk of an economic slowdown has increased. Much now depends on the actions of the President, the Federal Reserve, and Congress.

The Fed may offer some support by cutting interest rates, but its ability will depend on how inflation evolves. So far, Chairman Powell has been hesitant to commit to rate cuts. Meanwhile, Congress is working on tax-cut legislation. Because the tariffs are so impactful—enough to effectively negate the corporate income tax—lawmakers have room to provide substantial relief for both businesses and consumers. These policy decisions will be critical to watch.

We expect continued market volatility as investors react to ongoing developments. While most sectors have been affected, quality is beginning to stand out amid the chaos. We believe the best-positioned companies are those with pricing power, resistance to tariffs, innovative capabilities, strong leadership, and products or services essential to daily life. These businesses are more likely to weather the current storm and emerge stronger.

Thanks,
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S&P 500: Standard & Poor's (S&P) 500 Index. The S&P 500 Index is an unmanaged, capitalization-weighted index designed to measure the performance of the broad U.S. economy through changes in the aggregate market value of 500 stocks representing all major industries.