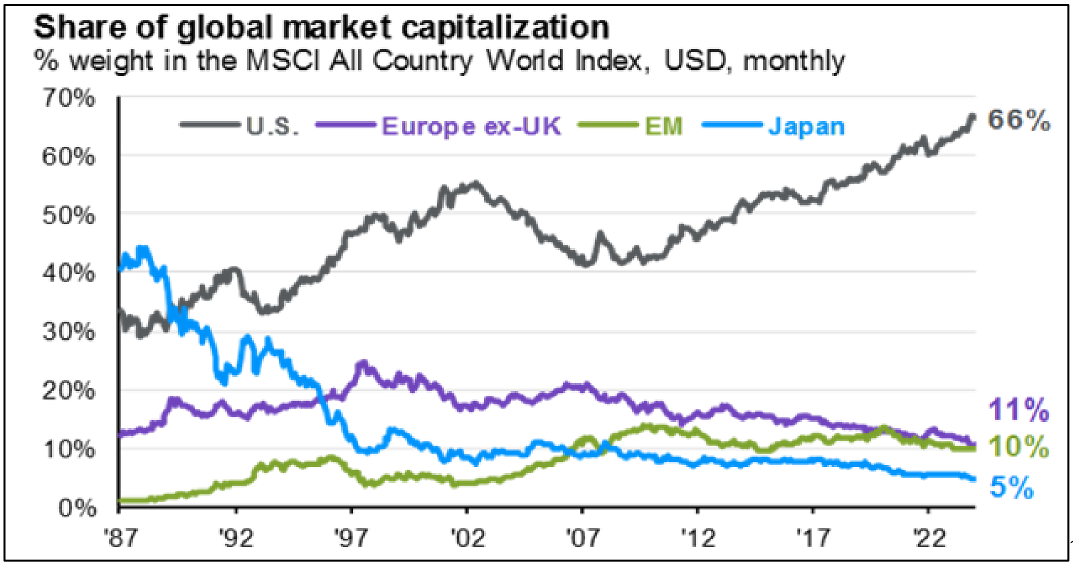
FOUNTAINHEAD ADVISORS

Market Commentary: The Repositioning of the US Empire

February 2025

In our commentaries we consistently wax poetic about America's dominant global position. In our December 2020 commentary, "Is Our Empire Crumbling?", we explored the nation's natural advantages - abundant energy and food, deep harbors, navigable waterways, and a strategic location between two vast oceans. More recently, we have highlighted America's entrepreneurial spirit, underpinned by a world class college system, robust capital markets and a free-market ethos envied by capitalists around the globe. It is one of the reasons our companies have dominated the information age as discussed in our January commentary, "AI and Valuations", and our associated podcast, "The Future of AI", with Tejas Dessai from Global X. Our collective advantages have led to a dominant position in global market capitalization.



[1]

Tune into our recent podcast "LA Fires – The Complexities of Insurance" featuring Jerry Theodorou, the director of the Finance, Industry, and Trade Policy program at the R Street Institute, a public policy research organization. We dig in to how past disasters have shaped the insurance industry and the implications of the LA fires on current insurance practices.

View this clip for a teaser.

Our podcasts are now also available on YouTube in video format as well as Spotify and Apple.

The market capitalization of United States of America (US) public companies now represents 66% of global public markets. This share peaked at just over 70% in the late 1960s before falling **below 30%** by the late 1980s.[2] Can the US maintain its current dominance or are we due for a decline back to 1980 levels?[3]

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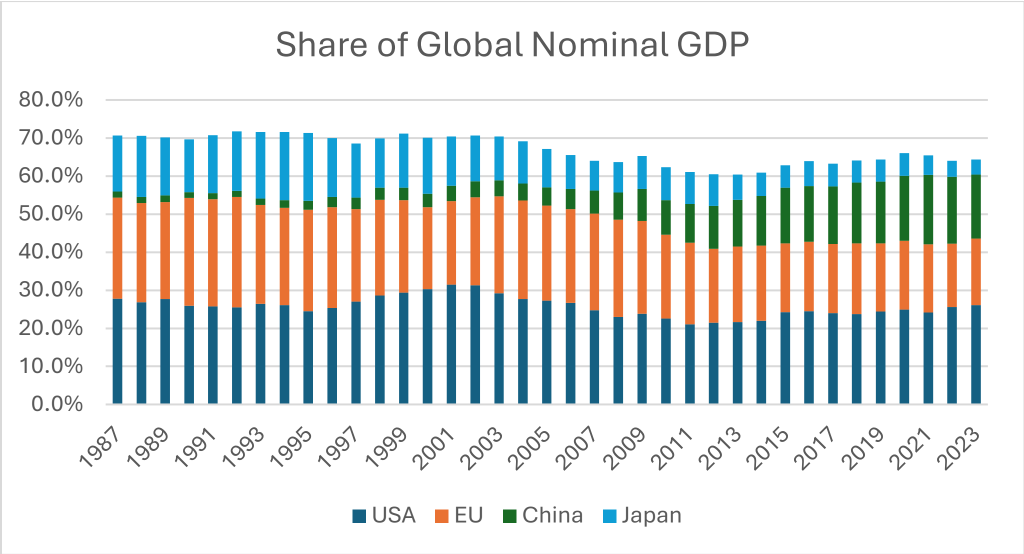
[1] JP Morgan Guide to the Markets as of January 31, 2025 – Page 43

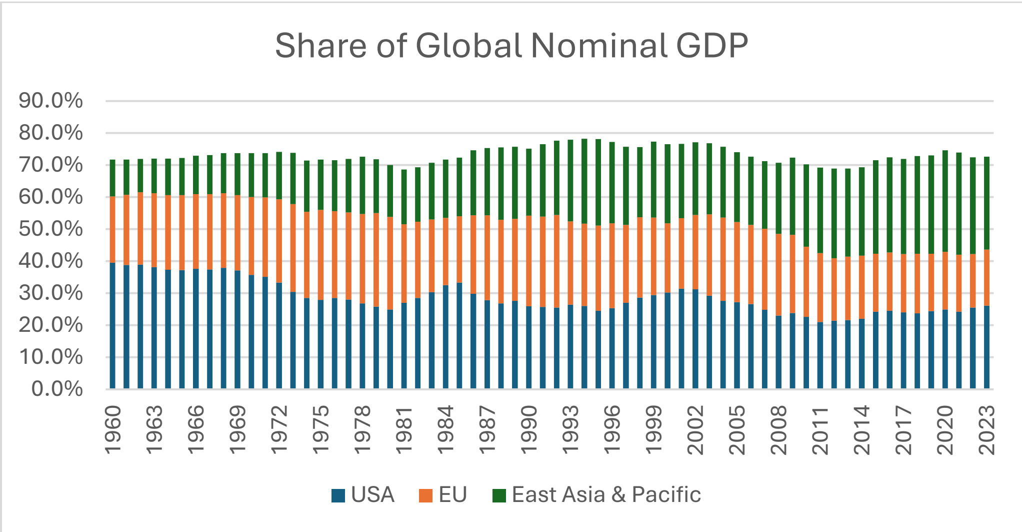
[2] Animation: Stock Market vs. GDP Share, by Country (1900-2022)

[3] It is worth noting that a drop in relative share of global markets does not necessarily mean poor US performance. For example, China can simply privatize government-led companies, resulting in a dramatic increase in public market capitalization but no real wealth creation. It's simply a category shift. Russia did this in the late '80s.

Moreover, while market capitalization shows U.S. dominance in global markets, it seems to contradict narratives surrounding tariffs that claim we are being taken advantage of in global trade. What gives? It may be that gross domestic product (GDP), which measures a country's output, offers a more comprehensive gauge of U.S. global standing.

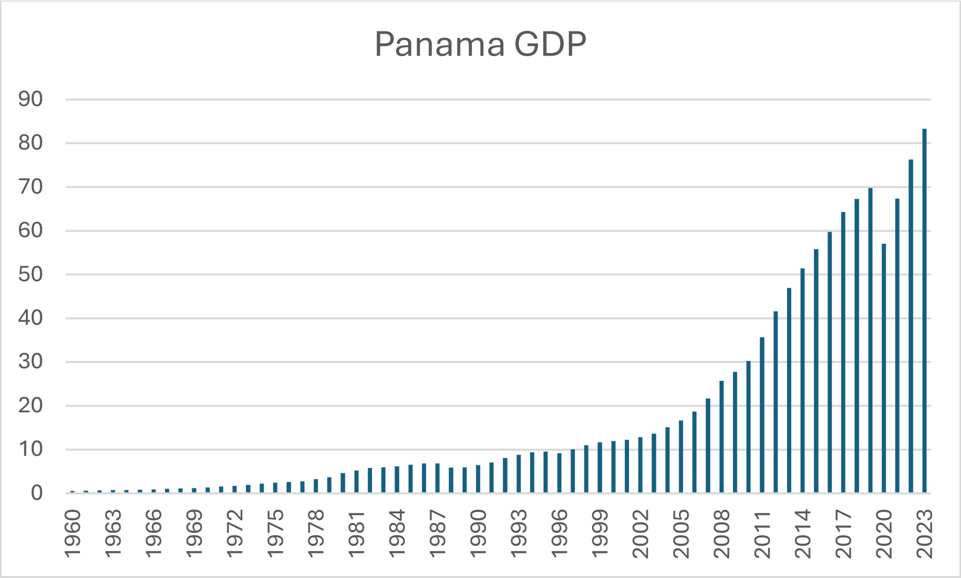


The US currently accounts for 26% of global GDP – a figure that sits in the middle of its 40-year range. Meanwhile, China has grown dramatically from their 2% share of world GDP in 1987 to 17% today. On the back of China, the Asia-Pacific region has taken on increased and growing importance from an economic perspective. As the chart below illustrates, the Asia-Pacific share increased from 11.5% in 1960 to 29% today, while the European Union's (EU) share dropped from 22% in 1960 to 17.5% today.



Deep Thought: American Power in Panama

American ingenuity resulted in the design and completion of the Panama Canal in 1914. That was after a failed effort by the French who were fresh off building the Suez Canal. America controlled the Panama Canal, as well as a 10-mile-wide canal zone alongside the actual canal, until its handover to Panama in 1999. In the interim, there were protests and riots against the American presence,[4] autocratic rule and, in 1989, the largest US military invasion since the Vietnam war when General Noriega refused to leave office. However, since the US helped depose General Noriega, governance in Panama has been rather good. As a result, Panama is prospering!



Having a secure, relatively wealthy country with strategic relevance (given the canal) who is friendly with the USA is beneficial from both a national security and economic perspective. Would Panama be as friendly if we kept the canal for ourselves?[5]

Should the USA have played a similar role in Venezuela by removing a dictator who refuses to adhere to election results or is that too much meddling? Should we try to aid those Venezuelans so they remain in their country, or should we put pressure on the countries between Venezuela and us – many of them our allies – to not allow passage? America has tried it all and there are no easy answers. Foreign policy not only

[4] One example: [The Panama Riots of 1964: The Beginning of the End for the Canal – Association for Diplomatic Studies & Training]

[5] The recent transaction where Blackrock purchased ports in Panama and therefore took them under a level of American control just may be enough for the Trump administration. It is important to note that Blackrock purchased these ports from a Hong Kong-based company – this is not America taking land from Panama. Along with the agreement signed in the late '70s by President Carter to return the Panama Canal in 1999 was a treaty highlighting neutrality with defense assurances by the USA. The current administration does not like strategic port locations controlled by foreign parties, particularly China-based ones.

affects national security matters (e.g., illegal migrants, view of America) but economic ones as well. For example, Venezuela is a petro-state in close proximity to the USA which can allow further abundance and efficiencies in our energy complex.

The Trump administration is cognizant of these realities – recognizing China as the foremost threat to our global position both economically and militarily and acknowledging the Asia-Pacific region's robust and growing economic presence. I recently had the privilege of attending an event featuring Terry Branstad, the former US ambassador to China, and David Adelman, the former US ambassador to Singapore, where they discussed "Tariffs, Trade and Trump 2.0."[6] In discussing the administration's stance on Ukraine and recent related events, these insiders revealed that high-level assurances of support were extended to our Asia-Pacific allies – such as Japan and South Korea – ensuring their security in the face of regional aggression. This illustrates a more nuanced approach to the world, one where we are selective rather than isolationist.

[7]

We have previously discussed what might be considered a bygone world order – one in which America policed global waterways, promoted globalization, and imposed a material cost for aggression towards neighbors. That reflects a more holistic and positive global view that general world prosperity would serve US interests.[8] Whether right or wrong, the Trump administration is rewriting those rules in favor of a more

[6] Sponsored by BTIG and Kraneshares
[7] AI generated via ChatGPT – DALL*E
[8] Perhaps a simplistic, naïve view given certain actions of the US over the last 80 years, but nonetheless an ideal that was strived for.

muscular, “America-first” approach. One of the ambassadors characterized this new direction by highlighting two key “isms” that are odds with recent US foreign policy:

- Protectionism
- Expansionism

Europe is on the outs. They are declining in economic importance, and they have been perceived by this administration as taking advantage of America, most notable through its failure to adhere to NATO’s guideline of allocating at least 2% of GDP to military defense spending.

America is signaling a more selective engagement with the world as can be seen with the administration’s differing stances in the Asia-Pacific region as compared to Europe. This approach is more transactional, as seen in our aggressive stance with regional allies Mexico and Canada. And perhaps surprising given the belief system of a large portion of the Republican/MAGA base, the administration’s approach will be expansionist as evidenced by early proclamations of interest in Panama, Greenland, and Gaza within the first 45 days of President Trump’s term.

Returning to the US share of global market capitalization, we can see a number of outcomes that are all interestingly positive for portfolio diversification. The Trump administration may have sped up significant change in Europe, as perhaps best exhibited by Germany’s recent budget overhaul.[9] Will US pressure help pull Europe out of its current malaise? Increased capital spend, lower regulations and other pro-growth initiatives might spur overall EU growth in both GDP and market capitalization. Moreover, higher tariffs combined with pressure on global companies - such as Taiwan Semiconductor’s (TSMC) chip investment in the US – to onshore manufacturing to the US, could boost US GDP while benefiting the market capitalization of the Asia-Pacific region. It could also address trade imbalances, another key focus of the Trump administration.

In short, while it may be challenging for America to maintain its current global dominance in market capitalization, this does not necessarily spell gloom and doom for our economy or indicate a declining market. Rather, it could reflect stronger international performance that ultimately benefits client portfolios through increased diversification.

[9] Germany's planned spending spree: what it means for the economy | Reuters

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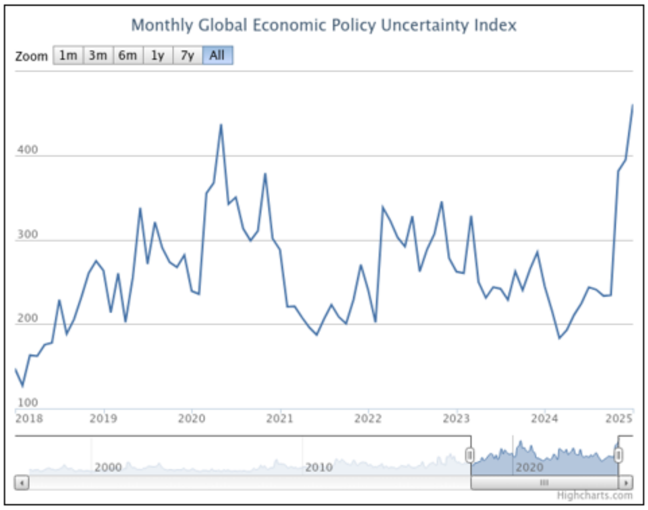
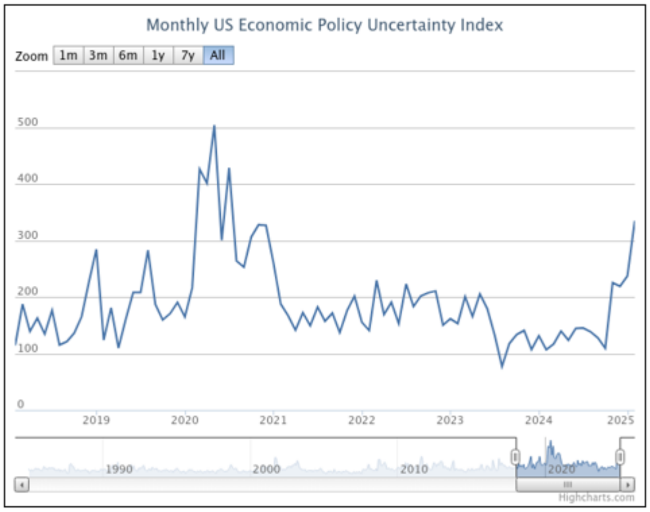
Talking Points: February 2025

Monthly Market Recap

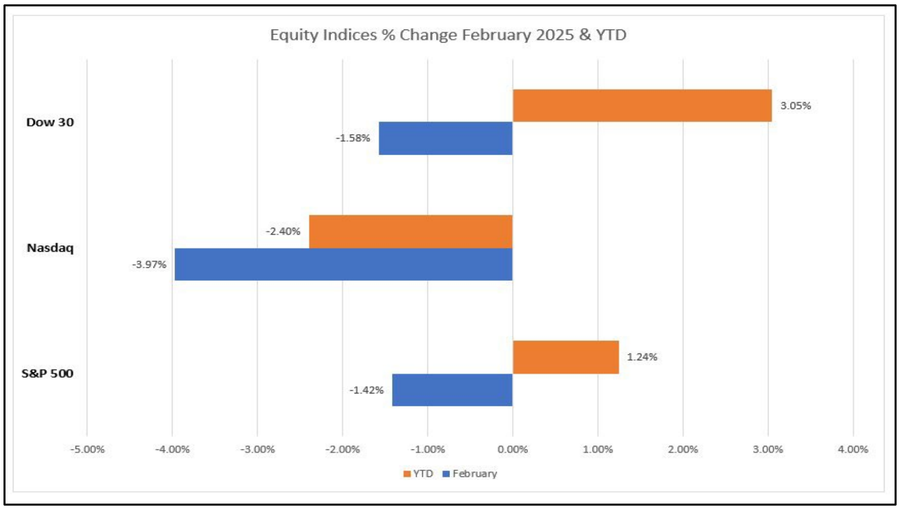
Part of what is affecting markets is uncertainty. Are we increasing tariffs on our neighbors longer term or not? What sectors may be carved out? Businesses will have a hard time planning which typically results in a freeze in capital investment. We are introducing an Economic Policy Uncertainty Index[10] to our monthly market recap. This index attempts to measure uncertainty within markets. Higher index levels correspond with higher uncertainty levels within the market, which is bearish. For example, the February US level is the highest on record outside of the initial stages of Covid.

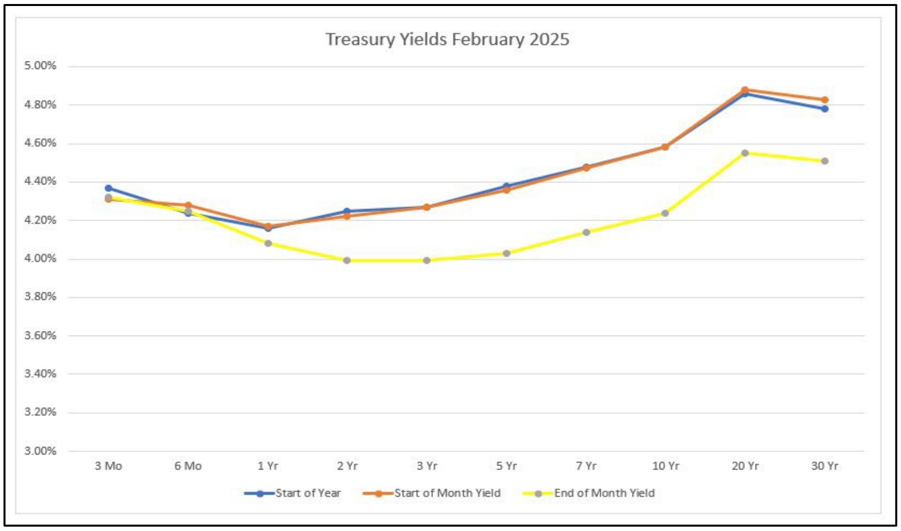




[10] Economic Policy Uncertainty Index
For methodology: https://www.policyuncertainty.com/methodology.html

Following the post-election rally, equity markets came to a screeching halt in February. All three major US indices were down, and yields declined sharply as investors' appetite for risk fell off a cliff. As of month's end, expectations remain that the Fed will not cut rates at its March meeting.





Much of February's negative performance can be attributed to concerns over the current state of the economy due to tariffs and general uncertainty given a very active Trump administration.

While consumer demand has remained surprisingly strong, resulting in company's earnings results having mostly beat forecasts, sentiment from both parties have declined recently:

- **Consumer sentiment data** released throughout the month showed a sharp decline relative to January and the end of 2024.

- **Company forward guidance** was much more bearish on the state of the consumer moving forward despite strong earnings for the quarter.

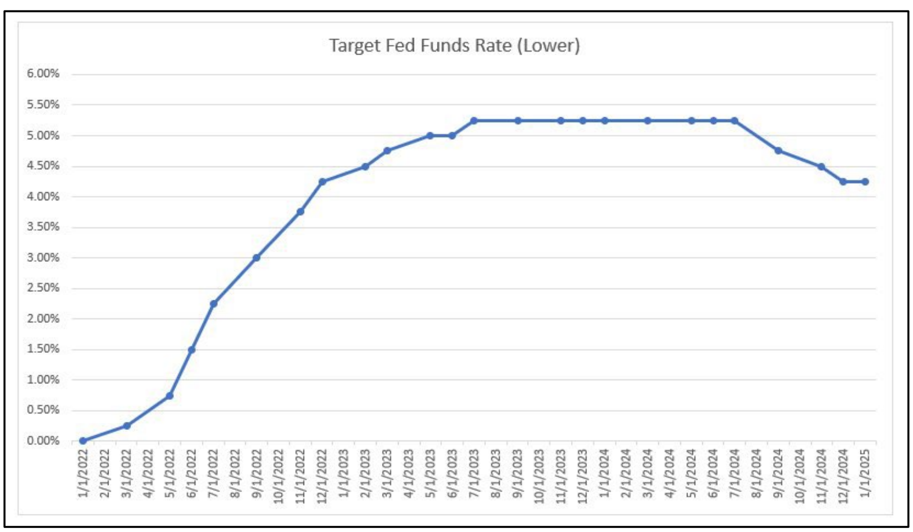
With tariffs on Mexico, Canada, and China set to go into effect in early March - and proposed tariffs on other countries and goods in the works - the risk is that these "concerns" become a reality. Tariffs are inherently inflationary, as companies will often opt to push these added costs onto the consumer by raising prices. If consumer spending falters as a result, companies' earnings will weaken leading to slowed economic growth for the economy as a whole.

Complicating matters further, rising inflation would severely limit the Fed's ability to cut interest rates. Like tariffs, interest rate cuts are inflationary in nature. Lowering rates reduces borrowing costs, encouraging spending and investment, which can push prices even higher. The silver lining in all of this is that while recent inflation data has flatlined, it has not yet reversed or shown a clear upward trend. Additionally, it is unclear how long these tariffs stay in effect or how broad they end up being - the Trump administration has already signaled a willingness to make deals with countries and sectors willing to work with them. Expect markets to be volatile as they continue to focus on tariffs and inflation throughout 2025.

January CPI and Core CPI (yoy)	*Jan.*	*vs. Expected*	*vs. Dec.*
CPI	*3.0%*	2.9%	2.9%
Core CPI	*3.3%*	3.1%	3.2%

January PCE and Core PCE (yoy)	*Jan.*	*vs. Expected*	*vs. Dec.*
PCE	*2.5%*	2.5%	2.6%
Core PCE	*2.6%*	2.6%	2.9%

Graphs/Visuals



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Probability of Upcoming Fed Interest Rate Decisions							
1/31/2025	*Hike*	*Hold*	*Cut*	*Hike 25bps*	*Cut 25bps*	*Cut 50bps*	*Cut 75bps*
March	0.00%	82.00%	18.00%	0.00%	18.00%	0.00%	0.00%
2/7/2025	*Hike*	*Hold*	*Cut*	*Hike 25bps*	*Cut 25bps*	*Cut 50bps*	*Cut 75bps*
March	0.00%	91.50%	8.50%	0.00%	8.50%	0.00%	0.00%
2/14/2025	*Hike*	*Hold*	*Cut*	*Hike 25bps*	*Cut 25bps*	*Cut 50bps*	*Cut 75bps*
March	0.00%	97.50%	2.50%	0.00%	2.50%	0.00%	0.00%
2/21/2025	*Hike*	*Hold*	*Cut*	*Hike 25bps*	*Cut 25bps*	*Cut 50bps*	*Cut 75bps*
March	0.00%	95.50%	4.50%	0.00%	4.50%	0.00%	0.00%
2/28/2025	*Hike*	*Hold*	*Cut*	*Hike 25bps*	*Cut 25bps*	*Cut 50bps*	*Cut 75bps*
March	0.00%	93.50%	6.50%	0.00%	6.50%	0.00%	0.00%

Highlights/Notes

Highlight: Concerns over tariffs and the current state of the economy led to a sharp decline in consumer confidence. This resulted in material selling pressure in equity markets - wiping out most of the gains from the post-election rally to start the year.

FAM Sentiment Summary 2024

2024	January	February	March	April	May	June	July	August	September	October	November	December
Fed	MILDLY BEARISH	MILDLY BEARISH	MILDLY BULLISH	BEARISH	MILDLY BEARISH	NEUTRAL	MILDLY BULLISH	MILDLY BULLISH	BULLISH	MILDLY BULLISH	BULLISH	MILDLY BEARISH
Interest Rate Decisions	NEUTRAL	n/a	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	BULLISH	NEUTRAL	BULLISH	NEUTRAL
Commentary	BEARISH	MILDLY BEARISH	BULLISH	BEARISH	MILDLY BEARISH	MILDLY BEARISH	MILDLY BULLISH	BULLISH	BULLISH	MILDLY BULLISH	MILDLY BULLISH	BEARISH
Economic Data	NEUTRAL	MILDLY BEARISH	MILDLY BEARISH	MILDLY BEARISH	NEUTRAL	MILDLY BULLISH	MILDLY BULLISH	NEUTRAL	MILDLY BEARISH	MILDLY BULLISH	NEUTRAL	NEUTRAL
Inflation	NEUTRAL	MILDLY BEARISH	BEARISH	BEARISH	NEUTRAL	BULLISH	BULLISH	BULLISH	MILDLY BULLISH	NEUTRAL	NEUTRAL	MILDLY BULLISH
Employment/Labor Market	MILDLY BEARISH	MILDLY BEARISH	MILDLY BEARISH	MILDLY BEARISH	BULLISH	NEUTRAL	MILDLY BULLISH	BEARISH	BEARISH	BULLISH	NEUTRAL	NEUTRAL
Housing/Real Estate	NEUTRAL	NEUTRAL	MILDLY BEARISH	MILDLY BULLISH	MILDLY BEARISH	MILDLY BEARISH	MILDLY BEARISH	NEUTRAL	NEUTRAL	NEUTRAL	MILDLY BULLISH	MILDLY BULLISH
GDP	BULLISH	n/a	NEUTRAL	BEARISH	MILDLY BEARISH	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	MILDLY BULLISH
Consumer Spending	MILDLY BEARISH	NEUTRAL	NEUTRAL	MILDLY BEARISH	MILDLY BULLISH	MILDLY BULLISH	NEUTRAL	MILDLY BULLISH	NEUTRAL	NEUTRAL	MILDLY BEARISH	MILDLY BEARISH
Consumer Sentiment	MILDLY BULLISH	NEUTRAL	MILDLY BEARISH	MILDLY BEARISH	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	MILDLY BEARISH
Global Events/News	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	MILDLY BEARISH	MILDLY BEARISH	MILDLY BEARISH	MILDLY BEARISH	MILDLY BEARISH	MILDLY BEARISH	MILDLY BEARISH	MILDLY BEARISH
China	MILDLY BEARISH	NEUTRAL	NEUTRAL	NEUTRAL	MILDLY BULLISH	NEUTRAL	MILDLY BEARISH	NEUTRAL	BULLISH	MILDLY BEARISH	MILDLY BEARISH	MILDLY BULLISH
Europe	NEUTRAL	NEUTRAL	MILDLY BULLISH	MILDLY BULLISH	MILDLY BEARISH	MILDLY BEARISH	MILDLY BEARISH	MILDLY BULLISH	NEUTRAL	MILDLY BULLISH	MILDLY BEARISH	NEUTRAL
Russia Ukraine War	NEUTRAL	NEUTRAL	MILDLY BEARISH	MILDLY BEARISH	MILDLY BEARISH	MILDLY BEARISH	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	MILDLY BEARISH	NEUTRAL
Israel Hamas War	NEUTRAL	NEUTRAL	NEUTRAL	MILDLY BEARISH	MILDLY BEARISH	MILDLY BEARISH	BEARISH	BEARISH	BEARISH	BEARISH	MILDLY BEARISH	NEUTRAL
US Politics	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	MILDLY BEARISH	MILDLY BEARISH	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	BULLISH	MILDLY BULLISH
2024 Election	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	MILDLY BEARISH	MILDLY BEARISH	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	BULLISH	MILDLY BULLISH
Budget Negotiations	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL
Earnings	NEUTRAL	MILDLY BULLISH	MILDLY BEARISH	NEUTRAL	BULLISH	MILDLY BULLISH	MILDLY BULLISH	NEUTRAL	NEUTRAL	MILDLY BULLISH	NEUTRAL	NEUTRAL
Banking Turmoil	MILDLY BEARISH	MILDLY BEARISH	MILDLY BEARISH	MILDLY BEARISH	NEUTRAL	MILDLY BEARISH	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL
Crypto	BULLISH	BULLISH	BULLISH	NEUTRAL	MILDLY BULLISH	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	NEUTRAL	BULLISH	BULLISH

FAM Sentiment Summary 2025

2025	January	February
Fed	**Mildly Bearish**	**Mildly Bearish**
Interest Rate Decisions	Neutral	Neutral
Commentary	Mildly Bearish	Mildly Bearish
Economic Data	**Mildly Bearish**	**Mildly Bearish**
Inflation	Mildly Bearish	Mildly Bearish
Employment/Labor Market	Bearish	Mildly Bearish
GDP	Mildly Bullish	Neutral
Consumer Spending	Neutral	Mildly Bearish
Consumer Sentiment	Neutral	Bearish
Housing/Real Estate	Mildly Bearish	Mildly Bearish
Global Events/News	**Mildly Bearish**	**Neutral**
China	Bearish	Neutral
Europe	Mildly Bearish	Neutral
Japan	Neutral	Mildly Bearish
Middle East	Neutral	Neutral
Russia/Ukraine	Neutral	Neutral
US Politics/Government	**Neutral**	**Bearish**
Tariffs	Bearish	Bearish
Economic Policy	Bullish	Neutral
Market Trends	**Mildly Bullish**	**Neutral**
Earnings	Bullish	Mildly Bullish
AI/Chips	Mildly Bullish	Mildly Bullish
Crypto	Mildly Bullish	Bearish

Noteworthy Details

- Consumer Spending - Neutral to Mildly Bearish
    - Even though markets did not have much of a reaction to data that showed retail sales from January came in lower than expected, concerns are building that consumer demand could start to weaken in 2025
- Consumer Sentiment - Neutral to Bearish
    - Sentiment was high post-election however consumers are now very concerned about tariffs
- US Politics/Government - Neutral to Bearish

- Markets remain bearish on all things tariff related, but this month offered less bullish news related to economic policy
- Crypto – Mildly Bullish to Bearish
    - Crypto bulls were riding high on hopes that this administration would help further bring the industry into the mainstream however this month investors became more cautious as sentiment weakened

Key Topics/Items from Below

- ***BEARISH***
    - January CPI and Core CPI data coming in higher than expected and higher than the prior month
    - "Unsettling" commentary from Walmart on guidance for the year citing concerns over weakening consumer demand
    - Trump announcing an additional 10% in tariffs on China (bringing the total to 20%)
    - Trump announcing that tariffs on Canada (25%), Mexico, (25%), and China (20%) would go into effect on March 4th.
    - The Conference Board's consumer sentiment index showing the largest month over month decline since August of 2021 as consumers grow increasingly concerned over the current state of the economy
    - Crypto currencies materially selling off due to investor concerns over the economy and a $1.4 billion hack of Bybit (large crypto exchange)
- ***MILDLY BEARISH***
    - The release of January's jobs report which showed that overall unemployment unexpectedly fell, and that the US added less jobs than expected (as a whole, pointing to continued labor market strength)
    - The release of The University of Michigan's consumer sentiment survey which showed that sentiment was at its lowest levels since July 2024 and inflation expectations at its highest levels since November 2023
    - Powell commenting after CPI data came in higher than expected (and higher than the month prior) that the US has "made great progress to bring down inflation" but that the job was not done yet
    - Trump proposing 25% tariffs on products like automobiles, semiconductors, and pharmaceutical products
    - The release of housing data which showed a 5% drop in existing home sales for the month of January
    - Bank of Japan commenting that it could raise rates this spring if the "domestic political situation worsens" (also cited concerns over US tariffs causing a "shock" to markets)

- Continued rise in natural gas prices (up over 160% vs. last year) driven by declining reserves and colder than expected weather
- Tesla reporting a significant decline in sales in Europe (stock performance down 45% vs last year)
- Ukraine and the US failing to reach an agreement on a mineral rights deal

- ***NEUTRAL***
  - China announcing several countermeasures in response to proposed US tariffs in the beginning of the month
  - Data released showing that the US trade deficit widened by more than expected in December
  - U.K. Central Bank announcing that it would be cutting rates this month in an attempt to spur growth and shore up the economy ahead of Donald Trump taking office
  - Powell commenting that he does not see "any reason to be in a hurry" when it comes to rate cuts for 2025
  - January PPI data coming in higher than expected
  - Retail sales data from the month of January coming in lower than expected
  - The release of the Fed's latest meeting minutes (where they opted to keep rates at current levels) which showed that officials debated the idea of slowing down or pausing the runoff of the nearly $6.8 trillion treasury reserves it holds
  - Microsoft announcing a breakthrough on a new quantum computing chip (powered by a "new state of matter" that is neither a solid, liquid, or gas)
  - Nvidia reporting better than expected earnings despite concerns over DeepSeek
- ***MILDLY BULLISH***
  - Better than expected earnings results from US retailers which pointed to the US consumer still being in "solid shape"
  - Treasury announcing that it would not be increasing debt issuance any time soon
  - President Trump announcing plans to impose 25% tariffs on all steel imports
  - The Trump administration opting to evaluate the use of "reciprocal tariffs" on several goods/countries rather than implementing broad based tariffs right away
  - Putin agreeing to begin talks with the US on a potential cease fire
  - Alibaba reporting stronger than expected earnings results citing Ai as a major catalyst
  - January PCE and Core PCE coming in line with expectations
  - Apple announcing that it would spend over $500 billion over the next four years in an effort to bring some of its manufacturing back to the US
- ***BULLISH***
  - Mexico and Canada coming to agreements with the US to delay implementation of tariffs in the beginning of the month

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