

Client Commentary | March 21, 2025

Market Commentary

Investing Insights

Recession Fears Have Re-Ignited

A little over a year ago, I wrote a Mitch on the Markets column about the growing likelihood of an ‘economic soft landing.’ I compared Fed policy and the economy in 2024 to what we saw in 1996, during the Greenspan Fed. Here’s what I concluded:

“In 1996, real GDP growth was volatile from quarter to quarter but rose 2.5% for the year, and the S&P 500 climbed +22.68%. I won’t be so bold as to call for a similar outcome in 2024, but the idea of modest GDP growth with solid double-digit gains in stocks does not seem out of the realm of possibility. In fact, I think it’s more likely than unlikely.”

I made my market call on the premise that the Fed and the U.S. economy would achieve an ‘economic soft landing,’ which went as hoped last year—the economy grew 2.8% and the S&P 500 rose +25%.¹

But 2025 looks a bit different out of the gates.

At the start of the year, investors were focused on the pro-growth, pro-business stance of the new administration. Many were pricing-in an era of lower taxes and deregulation, which consensus believed would drive M&A and economic growth higher. Confirmation of an ‘economic soft landing’ seemed all but assured.

But as initial policies began taking shape, confidence in a soft landing has somewhat dissipated. And recession fears have returned.

As I wrote last week, economic and trade policy uncertainty has spiked in the past few weeks. Many business leaders and investors assumed the administration would be sensitive to stock market volatility, perhaps pivoting policy in response. But that does not seem to be the case.

Treasury Secretary Scott Bessent has suggested that the U.S. may need a financial reset after years of government-driven expansion and rising asset values, and Commerce Secretary Howard Lutnick has

similarly noted that tariffs are likely to cause an initial surge in prices. The refrain is that the economy may need to endure some short-term hardship for long-term restructuring.

There's also the matter of reductions in the size of the federal workforce. The economic question to ask is whether the private sector will be able to fully absorb displaced workers at a time when businesses already face uncertainty over tariff policy. To be fair, the federal workforce declined by over 10% in the mid-1990s with no destabilizing effect on the jobs market, but that was also a time of steady, strong economic growth.

A final point to make in the recession argument is that household financial sentiment is showing signs of stress. A recent survey by the New York Federal Reserve recorded the most significant monthly decline in household confidence since 2023, while the probability of Americans missing debt payments has also risen to levels not seen since early 2020. These indicators suggest that economic unease is growing.

It is with this backdrop that the Federal Reserve must navigate its path on rates. Fed Chair Jerome Powell has signaled that policymakers are in no rush to adjust interest rates, and he has also hinted that the central bank may not immediately respond to tariff-driven price increases. For instance, if inflation accelerates further, the Fed will not necessarily rush to raise rates. They may opt instead to scrutinize data carefully, to distinguish between temporary price fluctuations and underlying inflationary trends. Fed Governor Christopher Waller described this as the challenge of "signal extraction," where policymakers must differentiate between short-term tariff effects and more concerning long-term inflation.

For investors, there are a lot of moving parts to consider.

BOTTOM LINE FOR INVESTORS

If I knew for certain that the Trump administration was going to levy 25% across the board, tariffs on all imports for one year (for example) or commit to implementing a 'reciprocal tariff policy' indefinitely, I could assign a much higher probability to near-term rising inflation, rising long duration Treasury bond yields, an economic recession, and a bear market.

The problem is that it's impossible to know how tariff policy will look tomorrow or at any point in the future.

Tariffs could be more permanent, which may hit economic growth slightly but potentially be offset by pro-growth policies like tax cuts and deregulation. The Trump administration could also pull back on tariff policy as the downside risks become more acute, which I think would factor as a positive surprise for markets. Again, there is no way to know for sure.

But now that recession fears have returned and are being telegraphed more frequently by major banks and financial media, I've become more optimistic. When recession fears return, the wall of worry follows—creating opportunities for positive surprises.

¹ Wall Street Journal. March 10, 2025. <https://www.wsj.com/economy/trump-team-recession-hard-landing-c8f23d5d>

STEADY INVESTOR WEEK

- **The Fed holds rates steady**
- **The 1960s ‘Chicken Tax’ and its lasting tariff impact**
- **Home sales in the U.S. rise unexpectedly**

The Fed Holds Rates Steady, Sees Slower Growth and Higher Inflation

The Fed did precisely what market participants were expecting. At its two-day policy meeting this week, the Fed opted to maintain its benchmark federal funds rate of 4.25% to 4.5%, as inflation’s downward progress has stalled and as elevated uncertainty stemming from recent policy changes has clouded the economic growth outlook. The Fed decision amounted to a “wait-and-see” posture, as more data is needed to see how inflation and growth trends may change in the coming weeks and months. In Chairman Jerome Powell’s words, *“We do not need to be in a hurry to adjust our policy stance, and we are well-positioned to wait for greater clarity.”* We tend to take Fed projections on the economy—and on the path of rates—with a grain of salt. Both are continually changing, and longer-term projects are usually off the mark. But it’s worth noting that the Fed lowered its GDP growth forecast for 2025 to 1.7% from the previously anticipated 2.1%, while expecting inflation to rise to 2.7%, primarily due to the impact of tariffs. The upshot is that inflation caused by tariffs can likely be ‘extracted’

from the component details, which would give Fed governors a clearer sense of underlying inflation trends. It could be that inflation ticks higher, but rates still come down, if the move higher in inflation is caused directly by tariffs and not structural forces in the economy. On the growth side of the Fed’s mandate, the decision to hold rates steady occurs against a backdrop of mixed economic indicators. While the labor market continues to exhibit steady hiring trends, consumer spending has shown signs of deceleration, suggesting a potential cooling of economic momentum. In response to these developments, the Fed has approved measures to slow the reduction of its asset portfolio, aiming to prevent potential strains in money markets and ensure sufficient liquidity within the financial system.¹

What the 1960’s-era “Chicken Tax” Teaches Us About Tariff Policy

For those who support tariff measures, the “chicken tax” may provide a useful case study. In 1964, the United States implemented a 25% tariff on imported light trucks, a measure known as the “chicken tax,” in retaliation against European tariffs on American poultry. The chicken tax effectively shielded domestic truck manufacturers from foreign competition, compelling international automakers to establish production facilities within North America to circumvent the tariff. This strategy ensured that popular models, such as pickup trucks, were produced domestically, thereby avoiding the substantial import duty. That’s the constructive argument for the tariffs. On the negative side, while the tariffs preserved some domestic manufacturing jobs, they also limited consumer choices and kept prices of certain vehicles higher than they might have been in a more competitive market.

Moreover, some companies resorted to creative measures, known as "tariff engineering," to bypass the tax. For instance, vehicles were imported as passenger cars and later modified into trucks to evade the tariff, highlighting the lengths to which manufacturers would go to mitigate its impact.²

Home Sales in the U.S. Rise Unexpectedly

The U.S. housing market has been in the doldrums for the better part of two years, but there have been bright spots. In February 2025, U.S. existing-home sales increased by 4.2% from the previous month, reaching a seasonally adjusted annual rate of 4.26 million units and widely surpassing economists' expectations of a 3.2% decline. This rise marked the first increase in two months, attributed to buyers acclimating to current mortgage rates, despite ongoing affordability challenges and elevated home prices. The national median home price rose 3.8% year-over-year to \$398,400, setting a record for February. Inventory levels increased by 5.1% from January and 17% compared to February 2024, totaling 1.24 million homes on the market. This data offers some signs of stability in the sector, but overall activity still remains subdued relative to previous years—especially those before 2023.³

¹ Wall Street Journal. March 19, 2025. https://www.wsj.com/economy/central-banking/interest-rates-decision-federal-reserve-ed172223?mod=economy_feat2_central-banking_pos4

² Wall Street Journal. March 19, 2025. https://www.wsj.com/economy/trade/the-1960s-chicken-tax-shows-the-lasting-impact-of-tariffs-aad04b6a?st=wLsgXF&reflink=desktopwebshare_permalink

³ Wall Street Journal. March 20, 2025. https://www.wsj.com/economy/housing/home-sales-february-2025-rise-f17edbfd?mod=hp_lead_pos1

DISCLOSURE

Past performance is no guarantee of future results. Inherent in any investment is the potential for loss.

Zacks Investment Management, Inc. is a wholly-owned subsidiary of Zacks Investment Research. Zacks Investment Management is an independent Registered Investment Advisory firm and acts as an investment manager for individuals and institutions. Zacks Investment Research is a provider of earnings data and other financial data to institutions and to individuals.

This material is being provided for informational purposes only and nothing herein constitutes investment, legal, accounting or tax advice, or a recommendation to buy, sell or hold a security. Do not act or rely upon the information and advice given in this publication without seeking the services of competent and professional legal, tax, or accounting counsel. Publication and distribution of this article is not intended to create, and the information contained herein does not constitute, an attorney-client relationship. No recommendation or advice is being given as to whether any investment or strategy is suitable for a particular investor. It should not be assumed that any investments in securities, companies, sectors or markets identified and described were or will be profitable. All information is current as of the date of herein and is subject to change without notice. Any views or opinions expressed may not reflect those of the firm as a whole.

Any projections, targets, or estimates in this report are forward looking statements and are based on the firm's research, analysis, and assumptions. Due to rapidly changing market conditions and the complexity of investment decisions, supplemental information and other sources may be required to make informed investment decisions based on your individual investment objectives and suitability specifications. All expressions of opinions are subject to change without notice. Clients should seek financial advice regarding the appropriateness of investing in any security or investment strategy discussed in this presentation.

Certain economic and market information contained herein has been obtained from published sources prepared by other parties. Zacks Investment Management does not assume any responsibility for the accuracy or completeness of such information. Further, no third party has assumed responsibility for independently verifying the information contained herein and accordingly no such persons make any representations with respect to the accuracy, completeness or reasonableness of the information provided herein. Unless otherwise indicated, market analysis and conclusions are based upon opinions or assumptions that Zacks Investment Management considers to be reasonable.

Any investment inherently involves a high degree of risk, beyond any specific risks discussed herein.

It is not possible to invest directly in an index. Investors pursuing a strategy similar to an index may experience higher or lower returns, which will be reduced by fees and expenses.

The ICE U.S. Dollar Index measures the value of the U.S. Dollar against a basket of currencies of the top six trading partners of the United States, as measured in 1973: the Euro zone, Japan, the United Kingdom, Canada, Sweden, and Switzerland. An investor cannot directly invest in an index. The volatility of the benchmark may be materially different from the individual performance obtained by a specific investor.

Zacks Investment Management, Inc. is a wholly-owned subsidiary of Zacks Investment Research. Zacks Investment Management is an independent Registered Investment Advisory firm that acts as an investment manager for individuals and institutions. Zacks Investment Research is a provider of earnings data and other financial data to institutions and to individuals.

This material is being provided for informational purposes only and nothing herein constitutes investment, legal, accounting or tax advice, or a recommendation to buy, sell or hold a security. Do not act or rely upon the information and advice given in this publication without seeking the services of competent and professional legal, tax, or accounting counsel. Publication and distribution of this article is not intended to create, and the information contained herein does not constitute, an attorney-client relationship. No recommendation or advice is being given as to whether any investment or strategy is suitable for a particular investor. It should not be assumed that any investments in securities, companies, sectors or markets identified and described were or will be profitable. All

information is current as of the date of herein and is subject to change without notice. Any views or opinions expressed may not reflect those of the firm as a whole.

Any projections, targets, or estimates in this report are forward looking statements and are based on the firm's research, analysis, and assumptions. Due to rapidly changing market conditions and the complexity of investment decisions, supplemental information and other sources may be required to make informed investment decisions based on your individual investment objectives and suitability specifications. All expressions of opinions are subject to change without notice. Clients should seek financial advice regarding the appropriateness of investing in any security or investment strategy discussed in this presentation.

Certain economic and market information contained herein has been obtained from published sources prepared by other parties. Zacks Investment Management does not assume any responsibility for the accuracy or completeness of such information. Further, no third party has assumed responsibility for independently verifying the information contained herein and accordingly no such persons make any representations with respect to the accuracy, completeness or reasonableness of the information provided herein. Unless otherwise indicated, market analysis and conclusions are based upon opinions or assumptions that Zacks Investment Management considers to be reasonable. Any investment inherently involves a high degree of risk, beyond any specific risks discussed herein.

The S&P 500 Index is a well-known, unmanaged index of the prices of 500 large-company common stocks, mainly blue-chip stocks, selected by Standard & Poor's. The S&P 500 Index assumes reinvestment of dividends but does not reflect advisory fees. The volatility of the benchmark may be materially different from the individual performance obtained by a specific investor. An investor cannot invest directly in an index.

The Russell 1000 Growth Index is a well-known, unmanaged index of the prices of 1000 large-company growth common stocks selected by Russell. The Russell 1000 Growth Index assumes reinvestment of dividends but does not reflect advisory fees. An investor cannot invest directly in an index. The volatility of the benchmark may be materially different from the individual performance obtained by a specific investor.

Nasdaq Composite Index is the market capitalization-weighted index of over 3,300 common equities listed on the Nasdaq stock exchange. The types of securities in the index include American depository receipts, common stocks, real estate investment trusts (REITs) and tracking stocks, as well as limited partnership interests. The index includes all Nasdaq-listed stocks that are not derivatives, preferred shares, funds, exchange-traded funds (ETFs) or debenture securities. An investor cannot invest directly in an index. The volatility of the benchmark may be materially different from the individual performance obtained by a specific investor.

The Dow Jones Industrial Average measures the daily stock market movements of 30 U.S. publicly-traded companies listed on the NASDAQ or the New York Stock Exchange (NYSE). The 30 publicly-owned companies are considered leaders in the United States economy. An investor cannot directly invest in an index. The volatility of the benchmark may be materially different from the individual performance obtained by a specific investor.

The Bloomberg Global Aggregate Index is a flagship measure of global investment grade debt from twenty-four local currency markets. This multi-currency benchmark includes treasury, government-related, corporate and securitized fixed-rate bonds from both developed and emerging markets issuers. An investor cannot invest directly in an index. The volatility of the benchmark may be materially different from the individual performance obtained by a specific investor.

The ICE Exchange-Listed Fixed & Adjustable Rate Preferred Securities Index is a modified market capitalization weighted index composed of preferred stock and securities that are functionally equivalent to preferred stock including, but not limited to, depository preferred securities, perpetual subordinated debt and certain securities issued by banks and other financial institutions that are eligible for capital treatment with respect to such instruments akin to that received for issuance of straight preferred stock. An investor cannot invest directly in an index. The volatility of the benchmark may be materially different from the individual performance obtained by a specific investor.