Taxes, Tariffs, and a Tumultuous Quarter

July 9, 2025

Tax and tariffs dominated the news through the second quarter. One uncertainty has been resolved, with the passage of the One Big Beautiful Tax Bill on July 4; the other continues to weigh on investors' minds.

Tax first. While there are several important wealth planning considerations associated with the new tax law (see our related article here), it is primarily an extension of the tax policy changes President Trump ushered in during his first term. Most economists expect the bill to be modestly stimulative to the economy over the next 12-18 months, as the additional business and individual tax cuts are to be implemented well ahead of the spending cuts. Some businesses should benefit, notably semiconductors manufacturers, defense contractors and airlines; others will be affected by loss of consumer subsidies on electric vehicles and tax credits for solar and wind projects. (Municipal bond tax-exemption and the private equity carried interest tax break were untouched.)

The bill primarily extended existing policy. In that context, the 10-year projected deficit declines modestly. Many media outlets have been characterizing the bill as a massive (by over $3 trillion) deficit expansion, but it is important to note that this is only relative to the scheduled expiration of the previous tax legislation.

While the bond vigilantes, who in the past have pushed long bond yields higher, acting as a governor for profligate fiscal and monetary policy, have been quiet as of late, the world is taking notice. After a period of real strength, the U.S. dollar has fallen over 7% against the Trade Weighted Dollar Index over the six months to June 30. This recent weakness may be a sign of a gradual shift away from the greenback as the global reserve currency, mostly due to U.S. policy. (We address this topic at length in our current edition of *Independent Thinking*.) Gold has been and will likely continue to be a beneficiary of this trend.

Meanwhile, trade remains a wild card, as evidenced again this week. The S&P 500 plunged 11% in the first week of April and international stocks also took a beating. Bonds offered no protection, falling modestly. Investors soon came to question Trump's real commitment to tariffs, however, and the markets recovered, with the S&P gaining 10.9% over the full quarter and both developed and emerging international markets (MSCI ACWI Ex-US Index and MSCI Emerging Markets Index) up over 12%. Bond yields and prices in the U.S. stabilized, generating a modest total return for the period. While Trump is back on the tariff trail, with new and renewed threats of steep tariffs announced on July 7 to take effect on August 1, the markets have so far held steady.

Investors are also focused on the economy and corporate earnings, which in the United States remain strong, although perhaps weaker than expected at the beginning of the year. Unemployment remains low, inflation continues to moderate, and capital investment, consumer spending and corporate earnings forecasts are all positive. At the same time, Artificial Intelligence-driven productivity enhancements are gathering steam, to a degree that should help support long term global growth.

As a result, betting market predictions of an imminent recession by Polymarket and others, which peaked in early April at close to 60% likelihood, have moderated meaningfully to a more normal figure of around 27%. The Federal Reserve seems to have interest rates at a level conducive to both stable inflation and economic growth.

In short, while some pressures have eased, uncertainty around the bigger picture remains high in aggregate. Geopolitical pressures and, in the United States, high levels of partisanship and unconventional policy, seem likely to continue. As long-term stewards of family and institutional wealth, we believe that thoughtful portfolio diversification remains essential.

CASH AND DEFENSIVE ASSETS

Taxable cash and cash equivalents continue to yield around 4%, meaning investors can still earn enough to keep up with the rate of inflation after tax. Intermediate and longer-dated municipal and corporate investment grade bonds also remain reasonably priced and we continue to incrementally extend the duration in these client portfolios as we believe prices are compensating investors for the risks associated with longer maturity bonds.

CREDIT ASSETS

Credit spreads (the yield differential between Treasuries and riskier corporate bonds) narrowed meaningfully during the quarter, leaving yields at the lower end of the recent range. The relative value versus higher quality bond investments is less appealing today than in the recent past. But if we avoid a recession, credit will still be an attractive investment over the medium term. We believe that investing in corporate credit remains a good long-term allocation within a diversified portfolio and that diversification within the credit asset class is prudent. For example, asset-backed loans seem to us an attractive addition at present to a balanced portfolio. The underlying range of collateral, such as residential and commercial real estate, auto loans, aircraft leases, and music and media royalties, is more diversified than corporate-backed loans and therefore less economically sensitive – and the exposure can generate high yields.

GROWTH ASSETS

At close to 22 times forward earnings, U.S. equity valuations are high, especially given the level of uncertainty. But modest near-term stimulative impact of the tax law and, more consequentially, the potential for an Artificial Intelligence-led productivity boom allows for a reasonable case for future, broad based margin expansion and wealth creation, which could keep valuations elevated for a prolonged period. The Magnificent Seven (Alphabet, Amazon, Apple, Meta, Microsoft, Nvidia and Tesla), which have been leading equities higher over much of the past decade, underperformed in the first half, rising 2% versus a 6.5% rise for the other 493.[1] We view this market broadening as a positive development, especially since most of the big technology stocks are still growing. We believe that most large companies will likely be beneficiaries of the productivity enhancements associated with the rollout of Artificial Intelligence.

International stocks strong performance reflects at least in part renewed optimism around fiscal stimulus, particularly focused on defense and infrastructure spending. The weak dollar has also provided a tailwind, as overseas equity positions have benefited predominantly from the rise in local currency and multiple expansion. We have maintained a significant underweight to international stocks for over a decade, but after years of U.S. equity outperformance, we have been selectively rebalancing equity exposure toward international stocks for clients, where appropriate.

[1] Yardeni Research

PRIVATE ASSETS

We continue to believe that a portfolio of private market investments, including private credit, private real estate, private equity and venture capital, can enhance portfolio returns while adding diversification.

Identifying high quality investment managers is essential, as private fund capital is locked up for a significant period and because the difference between the top quartile managers and the median manager in private equity is much greater than in public markets. An appropriately diversified portfolio of hard-to-access managers with strong track records is, we believe, an important addition to client portfolios with the appropriate risk appetite and liquidity profile. Private equity firms have been experiencing a more difficult fundraising environment and a more difficult exit environment. But with 87% of all U.S. companies with over $100 million of revenue still private, we believe a huge opportunity set remains for private equity firms able to raise capital today. We continue to work to ensure that our clients maintain sufficient liquidity when investing in private markets.

CONCLUSION

We are advising clients with equity allocations that have drifted toward the higher end of the range to rebalance lower while focusing on diversification in the underlying equity securities and managers and in international markets, but also by including other asset classes – high quality municipal and corporate bonds, liquid and semi-liquid credit, gold, and private alternatives.

We remain focused on helping our clients build portfolios that can withstand a range of economic and market scenarios, providing short- and medium-term liquidity, and satisfying long-term financial goals.

long-term investment horizons and provide limited or no liquidity. Sample assets in this class may include private equity, venture capital and illiquid real estate investments.