CROSSMARK
GLOBAL INVESTMENTS

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Crossroads Or Crosshairs?

Navigating Uncertainty, Tariffs, and Overvaluation

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This white paper is unusual for us in that it doesn't focus on a single topic, but a variety of subjects. Our decision to write at this juncture is attributable to the reduction in confidence and increase in uncertainty stemming from frequent and changing policy guidance from Washington, D.C. The stock market (S&P 500) went from an all-time high to a full-fledged correction (+10%) intraday in a month (during which time the NASDAQ fell +15% and the Magnificent 7 by nearly 20%). Risk assets despise uncertainty, and at this writing, there is plenty to absorb. We reiterate the cautious outlook we presented in releasing our 10 Predictions at the end of 2024. That caution was a result of some evidence of a slowing consumer and jobs market, a belief that earnings estimates were (and still are) too high, and that stocks were (and still are, to some degree) priced for perfection.

The correction

This was the fifth-fastest correction since World War II. The corrections that occurred more quickly than the current episode include the following:

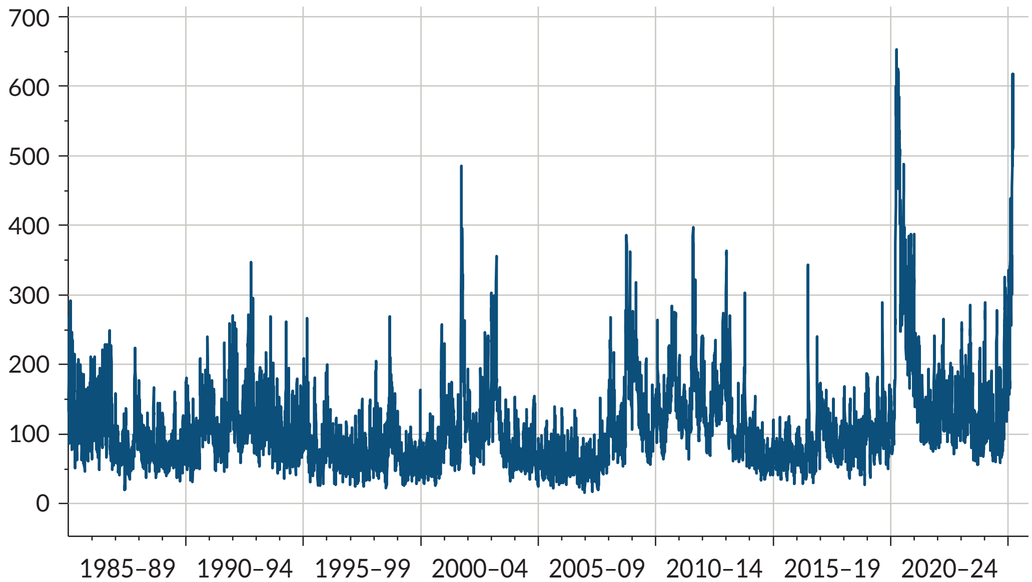
1. COVID-19 (February 2020)
2. Volmageddon episode (January/February 2018)
3. Temporary correction ~during the Asian Financial Crisis (October 1997)
4. Dot-com bubble (March 2000)

Causes of the correction include:

1. **Uncertainty. Risk assets despise uncertainty.** There was (and remains) plenty of uncertainty—tariffs, taxes, inflation, consumer spending, jobs, DOGE, etc. Some of this can be relieved by the administration, but most will take the passing of time.
2. **Tariffs.** Perhaps the main cause of the uncertainty is the tariffs—Who? What? When? How much? These questions need answers for businesses to properly plan and for markets to settle. (Inherently, we believe that in the short run, tariffs are not market-friendly as they are viewed as a tax and are inflationary. Longer term, there could be positives.)
3. **Overvaluation.** If you regularly read our weekly Doll's Deliberations or digested our 10 Predictions, you know we have been waving a red flag on valuations for some time. We also acknowledged that valuation is a very poor short-term timing tool and that markets need a catalyst for valuations to matter. Numbers 1 and 2 above were the catalysts.

U.S. Economic Policy Uncertainty Index

5-day moving average: 483.96[1]



CEO/CIO Richard Bernstein of Richard Bernstein Advisors writes: "Dramatically increased unpredictability is the cause of the market's recent volatility. The U.S. stock market is simply resetting its risk premium and valuation based on a sudden and broadening range of uncertain outcomes. Perceived uncertainty drives higher valuations, but policy fickleness drives multiple contraction."

There are various categories in which corrections are classified:

Garden variety pullback	**5–10%**
Normal, often unexplainable	
Growth scares	**10–20%**
Lowered confidence, elevated uncertainty	
Fear of systemic issue or recession that fails to materialize	
Examples: European debt crisis, U.S. debt downgrade	
Recession and wars	**25–33%**
Examples: The pandemic, 9/11, Gulf Wars	

1 Source: Bloomberg as of March 24, 2025

Economic observations

We have had (until the correction) one of the biggest momentum-driven bull markets since World War II. The momentum came as a result of AI enthusiasm, good economic performance, strong earnings results, and the prospect of Fed easing. This momentum move was aided by animal spirits post the election. This all peaked in the second week of February and reversed course quickly. The reversal was a result of a question mark about the pace of economic growth and policy actions of the new administration.

Heightened economic uncertainty is eroding consumer and business sector confidence and spending intentions. That the U.S. and world economy were in good shape is beneficial, as the near-run forecast is for just a slower growth rate. Had the global economy been weak heading into the trade war, then prospects would already be more worrisome. Still, the longer the uncertainty and tariff actions persist, the greater the recession risk. The economic backdrop may initially feel more stagflationary rather than outright recessionary. This is because the U.S. economy had considerable strength heading into 2025 and the rest of the world was slowly gaining momentum. As mentioned earlier, sticky inflation will be reinforced in the near run, unless upcoming damage trips the world into recession.

U.S. growth fears have mounted sharply in recent weeks, driven by the Trump administration's sizable enacted and proposed tariffs, its focus on reducing federal government spending, and an overall elevated sense of policy uncertainty/unpredictability. Incoming economic data have compounded these fears to an extent, with somewhat softer consumer spending in January, and the Atlanta Fed's popular tracking model indicating that the real GDP may contract this quarter. These factors have taken a toll on equities, which had been priced for solid growth, only modest and selective meaningful tariffs, meaningful deregulation, and expansionary fiscal policy.

The beginnings of a clear shift down in job gains is unfolding, likely to be exacerbated by DOGE job cuts, coupled with the surge in policy uncertainty and leading to declines in business and consumer confidence.

The Atlanta Fed's popular tracking model shows that GDP growth is on track to post a meaningful contraction (-2.4%) in 1Q. Amid the heightened policy uncertainty, the model's forecast has fueled the perception that U.S. economic activity has already started to soften markedly. However, the forecast of a contraction in GDP growth is misleading for several technical reasons. Correcting for these distortions, the Atlanta Fed's GDP tracking model indicates positive growth of 0.4% in 1Q, which may still underestimate 1Q growth. According to the betting markets, the probability of a recession in 2025 has risen from 20% to 35%.

The administration

In contrast with Trump 1.0, the President has led with isolationism and escalating trade tariffs, which has heightened economic uncertainty at home and abroad. We came into 2025 with a mild pro-growth stance, but warned that successful investment strategy would likely require periodic tactical shifts. It is premature to bet on a recession (outside of Canada), and recent turmoil may create a good buying opportunity in equities. However, for such an outcome to develop there will have to be a pivot in the U.S. to significantly lower trade uncertainty and a switch to pro-growth policies.

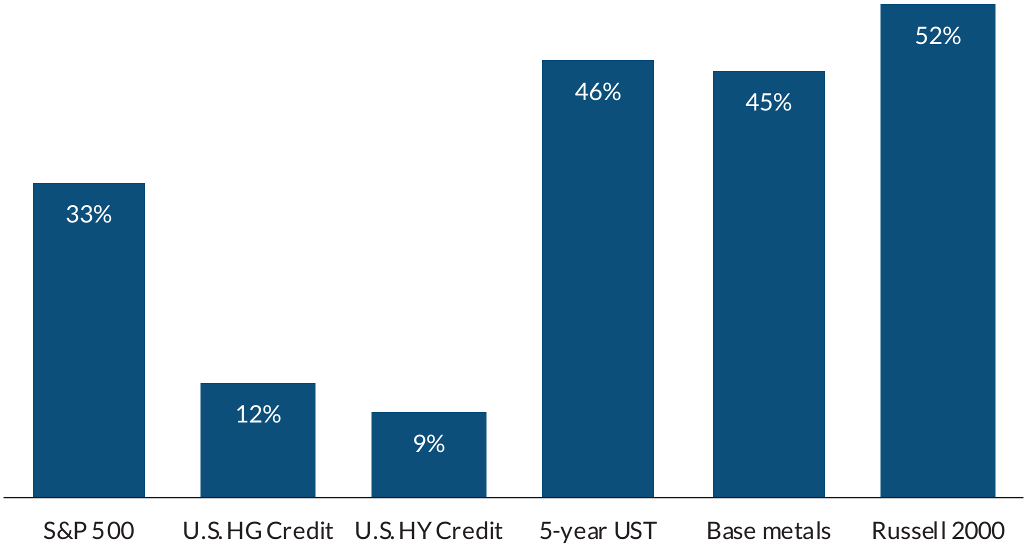
Donald Trump won the presidency on two key issues: 1) inflation and 2) immigration. More voters than not were willing to accept the chaos of a Trump presidency if it meant a stronger economy and a secure border. Trump has been able to secure the border, but the economy has gone in the other direction. Trump refused to rule out a recession and Commerce Secretary Lutnick said that a recession would be worth the structural changes. These types of comments can create self-fulfilling prophecies, as consumers and businesses hold back accordingly. Not coincidentally, Trump's approval rating nearly went underwater for the first time this term, and his economic approval rating is the lowest in any of his rankings ever.

Even though Trump is moving at warp speed, things take time to flow through the system and to change the economy and markets. Trump is changing everything, all at once, and the "big beautiful" bill is still far from done. We do not yet know how the tariffs will play out, what taxes will look like, how much Musk can cut, etc. It will take three to six months before we see how the economy is reacting and how the geopolitical situation is evolving. Some things will depend on how the courts rule on Musk, what tax bill finally passes, what spending cuts really happen, how the bond market reacts, what Iran and Putin do, what Xi agrees to. There are so many unknowns right now that forecasting is just a dart thrown in the air, not knowing where it lands.

Severe political acrimony is not helpful under current circumstances and is cited by some as a source of concern for resolving legislative standoffs as well as setting the tone for conciliatory actions. A Pew Research Center survey cited 63% of Democrats viewing Republicans as immoral, and 72% of Republicans viewing Democrats the same way. Nearly half of Americans consider members of the opposing political party to be "downright evil." Contrast that with the strong friendship between President Ronald Reagan and Speaker of the House Tip O'Neill. Reagan instructed his staff, "Remember we have no enemies, only opponents." (Enemies must be defeated; opponents are to be compromised with.)

The implied probability of recession from various markets is observable in the chart below. Remember, the probability of recession without any knowledge is about 15% (about the amount of time the economy is in a recession). Our best guess is that the probability of a recession in the last few months has risen from 20% to 35%. We note that continued reasonably tight credit spreads are a good sign recession risk is not great.

Implied probability of U.S. recession across asset classes[1]



We expect President Trump to ultimately pivot before the U.S. economy is dragged into a recession, but the administration's initial comments/actions have not been supportive of this view. A silver lining for the global economy arising from the trade war is that some laggard economies, particularly the euro area, are now planning on meaningful fiscal stimulus. And, for better or worse, defense spending is in a long-term bull market.

Tariffs

The Trump administration implemented a 25% tariff on imports from Canada (with the exception of energy imports tariffed at 10%) and Mexico, as well as an additional 10% tariff on China, increasing the effective tariff rate on the latter to 20%. Shortly after being enacted, a one-month delay was announced for imports of auto and related goods, as well as USMCA compliant goods, which represent a significant share of imports from these countries.

Strategas estimates that Trump's tariff plan will impose a $233 billion tax increase on the U.S. economy over the next 12 months, or 0.75% of GDP. In other words, all the benefits of moving from a 35% to a 21% corporate tax rate would be reversed by this tariff plan. Reciprocal tariffs are the least concerning to us, as we believe the threat of higher tariffs on certain products will force countries to negotiate. If we see countries lowering their tariff rates to avoid reciprocal tariffs, that would be positive for global growth.

Chief Global Strategist David Kelly of J.P. Morgan writes: "The trouble with tariffs, to be succinct, is that they raise prices, slow economic growth, cut profits, increase unemployment, worsen inequality, diminish productivity and increase global tensions. Other than that, they're fine. … Income taxes disproportionately hurt the rich. Tariffs disproportionately hurt the poor. … the U.S. does have a chronic trade problem, running a current account trade deficit every year since 1991. However, this largely reflects a too-high U.S. dollar, suggesting that gradually bringing the dollar down to a more competitive level, rather than raising tariffs, should be at the center of U.S. trade policy."

1 Source: JPMorgan as of March 11, 2025

Tariff implications

Near-term negatives

1. Price levels will increase with tariffs.
2. A significant number of new tariffs could act as an exogenous shock (like COVID), putting us into recession.
3. Corporate profit margins will likely get hit as tariffs hit.
4. Some consumer spending was accelerated into 4Q in anticipation of tariffs, setting the stage for a weaker 1Q/2Q.
5. Consumer and business confidence is declining.
6. Hiring and capital expenditure postponements are likely. (Layoffs and other delayed spending is likely.)
7. Tariff retaliation will aggravate economic stresses.

Potential longer-term positives

1. On-shoring continues/accelerates, providing U.S. jobs.
2. If tariffs become reciprocal in application, tariffs may fall.
3. Regulatory cutbacks may accelerate.

Deficits, inflation, the Fed, and bonds

Projected medium-term budget deficits are very high. The budget resolution recently passed by the House allows for a $4.5 trillion increase in the deficit due to tax cuts over the next 10 years, offset by $2 trillion decline in spending. Most of the $4.5 trillion in tax cuts (including an extension of the 2017 tax cuts) have been discounted by the market and so would not represent an additional boost for economic growth. This, combined with the accompanying proposed reduction in outlays, suggests that the composition of fiscal policy will be less pro-growth than in recent years.

Central banks may verbalize a return to a 2% inflation target, but we do not expect them to succeed. The surge in inflation over the past few years represents a clear break with the past four decades, when globalization and other forces kept consistent downward pressure on goods prices. Goods price inflation will generally be higher as companies build greater buffers into supply chains and selectively re-shore manufacturing. We expect the recent acceleration in wage costs to be sticky compared with recent decades, in part reflecting aging populations. Central banks may not formally abandon their current inflation targets, but they will not sacrifice growth to achieve them. We expect inflation in the U.S. to average approximately 3% in the next decade.

Investor risk-aversion should provide support for government bonds until the policy outlook is clearer. Heightened policy uncertainty will continue to boost demand for U.S. Treasurys as a hedge against slower U.S. economic growth. The U.S. 10-year Treasury yield continues to follow the expected Fed policy rate, which has recently drifted modestly lower in response to some U.S. economic growth concerns, and despite sticky U.S. inflation. We expect the Fed to be on hold until the Trump Administration's policy stance is clearer, but view near-term risks as biased toward easing. Past the short-term, the U.S. Treasury outlook remains challenging. With persistent above-target core inflation, there is little scope for Fed rate cuts.

Commodities

Gold prices are up sharply YTD and at an all-time high, with the latest run-up coinciding with the pullback in the U.S. dollar and rising U.S. policy uncertainty. Crude oil prices have slipped back to the lower end of their post-2022 range, reflecting both recent concerns about oil demand and a lingering supply overhang. From a trading standpoint, risks are to the downside as global economic growth expectations get scaled back.

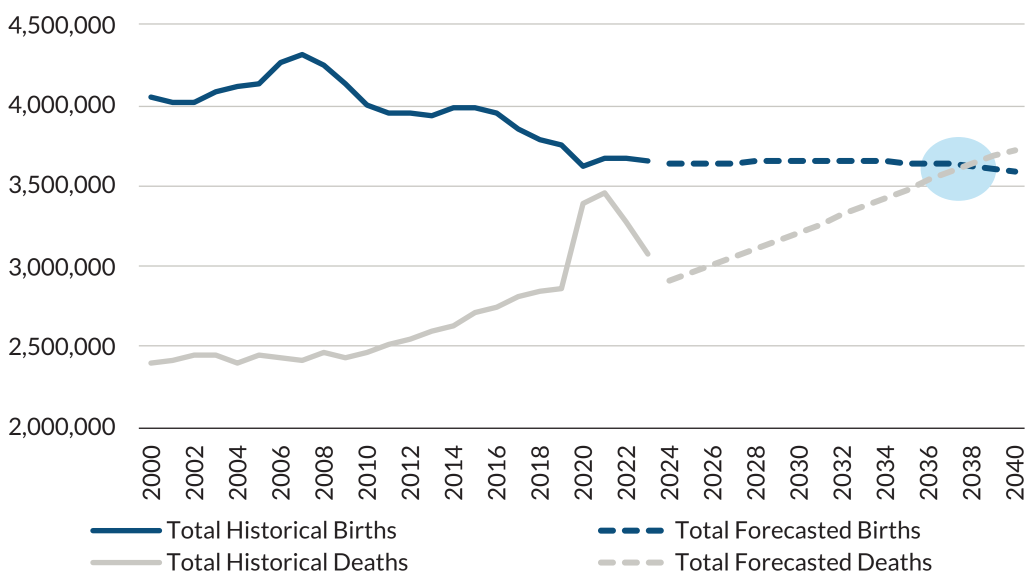
AI

Many investors have asked how they can tell whether AI is truly productivity-enhancing at the macro level to the degree that AI optimists believe. It seems clear that AI is a useful technology that will be used by consumers and businesses; the question is to what extent and effect. U.S. equities are overvalued if AI does not lead to a substantial boom in U.S. productivity, underscoring the profound risk facing equity investors if the narrative about AI shifts in a pessimistic direction.

Demographics

Demographics, while sometimes like watching paint dry, can have significant long-term implications. The gap between births and deaths is continuing to shrink, with almost all of our recent population growth coming from immigration. Going forward, as immigration is dramatically curtailed, overall population growth could turn negative by the middle of the next decade, while the working-age population would immediately start to contract.

Historical and forecasted U.S. births and deaths by year[1]



An America with less population growth would see weaker demand growth overall but particularly for housing and basic consumer goods and services. Moreover, if the working-age population begins to fall before the overall population, supply would be hit more than demand, potentially boosting wages, inflation, and interest rates but also motivating even stronger investment in productivity-enhancing AI and robotic technologies.

1 Sources: U.S. Census Bureau (Population Division), National Center for Health Statistics

Earnings, valuations, and stocks

2025 consensus earnings estimates started the year at +14%. That number is now 10%, with first- and second-quarter estimates reduced by 6% and 3%, respectively, and hardly any changes to the back half of the year. We expect further reductions in earnings estimates due to economic weakness.

Valuation levels remain high

S&P 500 valuation: Current percentile ranking relative to history[1]

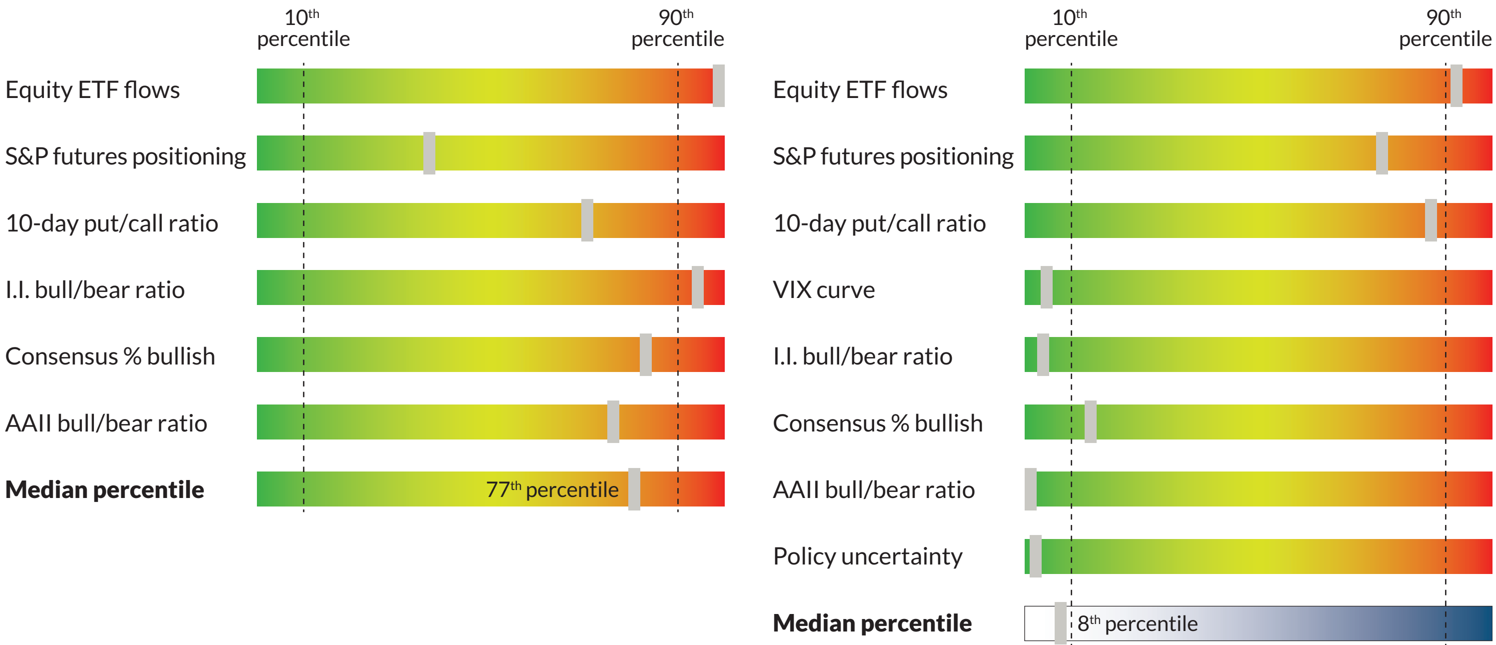
Given the elevated uncertainty around trade policy, and the Administration's recent rhetoric indicating a tolerance for some near-term economic weakness to achieve trade goals and other objectives, concerns about meaningful downside risks to growth are valid. We expect volatility to remain elevated (see Prediction #5) as uncertain crosscurrents continue.

1 Source: Strategas

Sentiment is an important indicator of potential future market direction. As recently as three months ago, sentiment was running strong (at concerning levels—see left chart below). Currently, almost the opposite picture prevails (see right chart below). This is a significant shift in a short amount of time, arguing for at least an oversold rally.

Strategas sentiment dashboard: Current reading vs. historical range[1]

Dec. 13, 2024 | March 17, 2025



Our 6099 year-end S&P target is lower than any of the Wall Street strategists (see below), and if accurate, will record a down year, but would require a nice rally from current levels. After the “vicious” rally we are calling for that would take the S&P to the upper 5000s, we expect a test back to 5500 [the area of the recent low (or maybe 5200-5400)]. After that, the trajectory of the economy and earnings will be key.
If the economy is okay, that could be the low for the year. Conversely, if we experience a recession, the S&P 500 could sport a “4” handle. After two back-to-back years of approximately 25% returns, 2025 is shaping up to be a much more difficult year in which to make money.

1 Source: Strategas

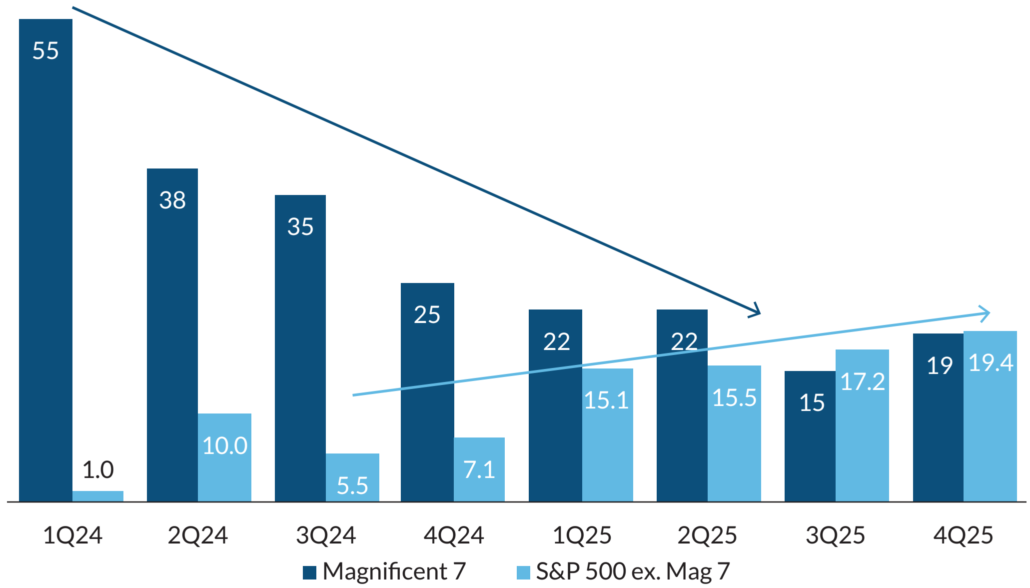
Year-end 2025 Wall Street strategist targets[1]

Firm	Px target
Wells Fargo	7,007
Yardeni Research	7,000
Deutsche	7,000
BMO Capital Markets	6,700
Nataxis	6,700
HSBC	6,700
BofA Securities	6,666
Barclays	6,600
RBC	6,600
CFRA	6,585
Goldman Sachs	6,500
Morgan Stanley	6,500
BNP	6,300
Average	6,681
S&P on 12/27/24	5,970
% difference	**11.90%**

Equal-weighted portfolios are likely to beat cap-weighted portfolios, especially as Magnificent 7 earnings growth slows and the other 493 earnings growth improves.

1 Source: Strategas

Mag 7 earnings are expected to slow, while other 493 earnings are expected to accelerate[1]



A summary of our premises and expectations

2025 premises[2]	Expectations going forward include
1. The U.S. to remain the global growth engine.	1. U.S. growth is slowing, but hopefully avoids a recession.
2. The business cycle, while advanced, continues to expand.	2. The job market is likely to experience further weakness.
3. The Fed and other central banks are poised to lower rates further.	3. Earnings estimates remain too high.
4. AI is driving a CapEx boom.	4. Trade policy pronouncements need to quiet down for confidence to rise and uncertainty to fall.
5. A more favorable regulatory backdrop should aid business growth.	5. Reciprocal tariffs versus uniform or punitive tariffs would be welcome.
6. More oil supply will likely lower energy prices.	6. Inflation is likely to remain closer to 3% than the Fed's 2% target.
7. Earnings growth should broaden.	7. Key to avoiding a recession will be the extension of the expiring Trump tax cuts after Dec. 31.
8. Possible policy actions and executive orders create considerable uncertainties.	8. DOGE efforts will continue with some, but limited success.
9. Equity valuation levels are very high.	9. Hopefully, volatility quiets some, but is likely to remain above average.
10. Higher equity volatility and dispersion are likely.	10. Diversification will be important this year (i.e., own some value and international).
11. A large renovation of federal government will be attempted.	
12. Foreign policy will be "America first."	

1 Sources: JPMorgan, Crossmark
2 Sources: BofA US Equity & Quant Strategy, FactSet

Longer term

Total returns on balanced portfolios of publicly listed assets over the next 10 years will be below the norms of recent decades, given elevated current valuations and what we expect to be moderate global economic growth and higher inflation. There are many sources of uncertainty about the economic outlook, but one thing is certain for prospective returns: The tailwind of falling inflation and interest rates that prevailed for most of the past 40 years has ended. That tailwind boosted valuations for virtually all assets and allowed central banks to cut policy rates in response to economic or capital market weakness. Thus, the past is not prologue. Equities (and to some degree, bonds) are expensive by historical standards, tempering potential returns in the years ahead.

S&P 500 average forward returns (%)[1]

Starting P/E	1-year	3-year	5-year	10-year
<10x	13.4	11.2	12.3	11.5
10–12	14.9	13.0	10.4	10.5
12–14	10.5	9.1	8.5	9.6
14–16	12.4	10.9	9.8	9.3
16–18	6.4	6.3	5.4	5.7
18–20	7.7	6.0	5.9	4.4
>20	5.2	4.8	5.5	3.0

10-year return forecast

Asset class	Range (%)
Equities	**5–7**
U.S.	4–6
Non-U.S. developed markets	5–7
Emerging markets	5–7
Bonds	**2–4**
U.S. government	2–4
U.S. investment grade	3–5
U.S. high yield	4–6
Emerging market sovereign	3–5
Cash	**4–6**
Inflation	**4–6**

1 Source: Strategas

About Crossmark Global Investments

Crossmark Global Investments is a faith-based investment management firm that creates and manages values-based investment strategies with a goal of providing performance excellence for financial intermediaries and their clients. Founded in 1987, the firm specializes in developing tailored solutions and has a rich history of inspiring and equipping its clients to align their investments with their values. For more information, visit crossmarkglobal.com.

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