02.11.2025

Campaign Rhetoric vs. Governing Reality

Our Take on President Trump's Economic Policies

by ADAM GROSSMAN, CFA

THE WRITING TEAM

ADAM GROSSMAN, CFA
Global Equity CIO | Partner

CHRIS KONSTANTINOS, CFA
Managing Partner |
Chief Investment Strategist

KEVIN NICHOLSON, CFA
Global Fixed Income CIO | Partner

ROD SMYTH
Chairman of the Board of Directors

DAN ZOLET, CFA
Associate Portfolio Manager

SUMMARY

- Headline-grabbing policies from a new administration are normal, and often create uncertainty, in our view.
- Historically, economic policy proposals that are not rooted in broad support tend to hit obstacles.
- Many of Trump's early policies seem to be destined for compromised implementation as law, or as temporary executive orders; this may blunt their long-term impact.

Depending on one's political views, we think it is natural to hope -or fear - that politicians will institute their campaign promises. Only three weeks into the Trump presidency, it is admittedly too early to assess the impact of even his first 100 days in office, much less his second term. However, we wanted to use this *Weekly View* to apply our "process over prediction" mantra to the analysis of his proposed agenda.

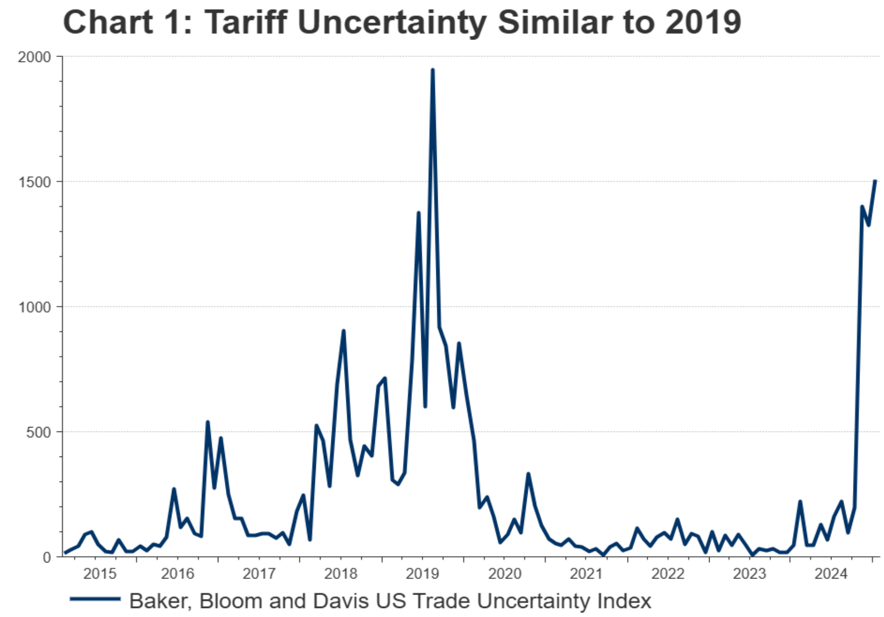
At RiverFront, our job is not to say what politicians should do… but rather to seek to understand the economic and market impact of what they *actually* do. In that light, a key takeaway from our study of US political history is that "divided we stand" is a useful mantra for investors trying to incorporate the impact of politics on markets. We hope to illustrate this by contrasting campaign rhetoric and early plans of previous administrations with the reality faced once in office.

We believe that these 'history lessons' – provided later in this piece – demonstrate how our government's separation of powers provides a natural governor on policies that may have been popular on a campaign trail but are less practical in execution. To that end, **our emerging take is that many of President Trump's proposals represent novel, aggressive negotiating tactics that may have difficulty being implemented in full.** With this context, here is our early view on what is more or less likely from President Trump's administration from an economic policy standpoint:

Tariff Policy: The President is allowed to levy tariffs for up to 150 days, unless he declares a national emergency. Given this, we continue to believe that tariffs are more likely a negotiating tactic for Trump to achieve other goals such as immigration reform and drug trafficking reduction. The 11th hour concessions from Mexico over border control last week seem to corroborate our view. This also illustrates how important it is for investors not to react too quickly to any one pronouncement. Our view is that tariffs have little mainstream economic support and are likely to fall hardest on Trump's voter base. The major exception to this is policy towards China, as we believe that there is considerable support in both parties for maintaining an adversarial economic stance.

Tax Policy: While tax cuts of various kinds have been floated over the past several months, the reality we see is that higher interest rates are going to put pressure on our deficits and total debt burden. Given this and the fact that tax policy must go through Congress, major personal tax cuts seem unlikely to us. However, extending the existing tax breaks via the Tax Cut and Jobs Act (TCJA) for another 10 years are likely and if so, stimulative to the economy. One potential bipartisan 'wild card' tax cut might be a partial repeal of the State and Local Tax ('SALT') deduction cap, although support on the Republican side for this has been spotty.

Energy Policy: The permanence and extent of Trump's energy policies will likely be dependent on inflation, in our view. While energy policies certainly have an influence on energy prices, so do geopolitical events and a variety of economic factors. Lower energy prices are an important input to inflation, but there are numerous other factors as well. If administration policy is perceived to have delivered lower inflation, then those polices are likely to become more permanent.



Source: LSEG Datastream, RiverFront. Data monthly as of January 25, 2025. Chart shown for illustrative purposes. Not indicative of RiverFront portfolio performance. Index definitions are available in the disclosures.

We will attempt to handicap all these policies as their impacts on interest rates and earnings become clearer. The reality we face, in the short term, is that Trump's approach, especially around tariffs, has elevated uncertainty in markets (see Chart 1, right). As a result, we have reduced international equity exposure in all our portfolios. In addition to uncertainty, we are seeing the anticipated effect of his policies in the relative price action of sectors and the stock market overall. Since we do believe that Trumps policies on aggregate will drive faster nominal growth in the US, we have a larger weight in Small Cap US, which we believe are more economically sensitive in the longer horizon portfolios.

History Lesson #1: Executive Orders and Agency Enforcement Are Easy to Enact… But Not Enduring

In the last 25 years, executive orders have become a popular tool for policy creation, despite likely being overturned by future administrations. However, there are a few key reasons this is less effective than it might appear:

- **Lack of Permanence:** Executive orders typically have at most an eight-year shelf life if they do not enjoy some bipartisan support. This is specifically of note for economic or tax policy where we believe a sense of permanence is important to drive long term behavior.

- **Legal Interpretation:** In May of 2024, the Supreme Court reversed a concept known as the 'Chevron Deference'. This doctrine allowed the executive branch wide latitude to enact legislation through enforcement in cases where Congressional mandates on specific laws were not clear. We believe the implications of this change in legal interpretation is profound, given how much it likely limits executive authority for long term policies. This shift will limit the duration of practices seen as overreach by executive branch agencies, as well as making new regulation harder to enact and more limited in scope, in our opinion.

History Lesson #2: Enduring Policy is Usually Broadly Supported

While it is our view that elections have consequences on economic policy, it is also evident that lasting policies in recent history have required some modicum of bipartisan support. Looking at the last thirty years provides numerous examples to corroborate our thesis. A great example is the George W. Bush tax cuts. In 2001, the Bush administration was able to push his tax cuts through with votes from both parties, with additional provisions added in 2003. However, he had to settle on a $1.35 trillion tax cut after seeking $1.6 trillion. Further, many of the core elements of the Bush plan survived the Obama "blue wave" and tax policies. And while President Obama's initial attempt at getting the Affordable Care Act through a Democratic Congress were stalled, he ultimately took the route of compromise and succeeded in meaningful health care reform that is still in place today.

Similarly, Trump's pair of protectionist policies from 2018, the original China tariffs and ending engagement with the Trans-Pacific Partnership (TPP), both ultimately received at least enough lukewarm support to not be overturned. President Biden took up the baton against China, using outright industry bans in lieu of tariffs, which have also received enough support to remain in effect (thus far) through the transition to the new administration.

History Lesson #3: Going It Alone Has Proven Ephemeral for Economic Policy

Recent history also shows that many of the more non-consensus ideas that don't enjoy bipartisan support tend to have execution challenges, even with a majority in both houses. Given the current make up of Congress, it only takes 4 senators or 7 representatives from the majority to stop a controversial piece of legislation in its tracks. Early examples that are instructive were healthcare under President Clinton and entitlement reform under President George W Bush. Clinton's push for what was known popularly as 'Hillary Care' failed to get to any meaningful reform despite a Democratic majority in both houses. Bush's second term attempt to privatize Social Security lacked bi-partisan support and failed to gain any traction before the Republican majority was voted out in the 2006 midterms.

More recently, President Trump's attempts to overturn the Affordable Care Act were stalled by fractures within his majority as well. This ended up being a mirror image of the challenges President Obama had with the Affordable Care Act, which required significant compromises to come into law despite a Democratic majority in both houses at the time. Along the same vein of thought, President Biden, with a majority in both houses, found his original Inflation Reduction Act unpalatable to a few key senators and was forced to compromise on many key provisions.

Portfolio Implications: Volatility Now, Economic Impact Later

We are prepared to take further action in our portfolios if we see the potential for an enduring change in the outlook for sectors and markets overall, and to make risk management actions if important technical levels are breached. What is not yet clear, and likely won't be for a least a quarter as earnings data comes in, is the impact of abrupt shifts in policy on corporate activity and earnings. Uncertainty has the potential to slow earnings growth, but since earnings growth has remained strong, it is too early to tell whether the volatility expressed in the market is simply reflecting uncertainty or if it is predicting earnings challenges.

In summary, enduring policy changes can have a lasting impact on markets. Our mantra is 'policy over politics' and so we will be seeking to avoid reacting to rhetoric, but instead to understand what policies will be enacted by Congress or made through executive orders, which ones will be enduring, and what their impact will be on markets.

Risk Discussion: All investments in securities, including the strategies discussed above, include a risk of loss of principal (invested amount) and any profits that have not been realized. Markets fluctuate substantially over time, and have experienced increased volatility in recent years due to global and domestic economic events. Performance of any investment is not guaranteed. In a rising interest rate environment, the value of fixed-income securities generally declines. Diversification does not guarantee a profit or protect against a loss. Investments in international and emerging markets securities include exposure to risks such as currency fluctuations, foreign taxes and regulations, and the potential for illiquid markets and political instability. Please see the end of this publication for more disclosures.

This report does not provide recipients with information or advice that is sufficient on which to base an investment decision. This report does not take into account the specific investment objectives, financial situation or need of any particular client and may not be suitable for all types of investors. Recipients should consider the contents of this report as a single factor in making an investment decision. Additional fundamental and other analyses would be required to make an investment decision about any individual security identified in this report.

Chartered Financial Analyst is a professional designation given by the CFA Institute (formerly AIMR) that measures the competence and integrity of financial analysts. Candidates are required to pass three levels of exams covering areas such as accounting, economics, ethics, money management and security analysis. Four years of investment/financial career experience are required before one can become a CFA charterholder. Enrollees in the program must hold a bachelor's degree.

All charts shown for illustrative purposes only. Technical analysis is based on the study of historical price movements and past trend patterns. There are no assurances that movements or trends can or will be duplicated in the future.

Stocks represent partial ownership of a corporation. If the corporation does well, its value increases, and investors share in the appreciation. However, if it goes bankrupt, or performs poorly, investors can lose their entire initial investment (i.e., the stock price can go to zero). Bonds represent a loan made by an investor to a corporation or government. As such, the investor gets a guaranteed interest rate for a specific period of time and expects to get their original investment back at the end of that time period, along with the interest earned. Investment risk is repayment of the principal (amount invested). In the event of a bankruptcy or other corporate disruption, bonds are senior to stocks. Investors should be aware of these differences prior to investing.

In general, the bond market is volatile, and fixed income securities carry interest rate risk. (As interest rates rise, bond prices usually fall, and vice versa). This effect is usually more pronounced for longer-term securities). Fixed income securities also carry inflation risk, liquidity risk, call risk and credit and default risks for both issuers and counterparties. Lower-quality fixed income securities involve greater risk of default or price changes due to potential changes in the credit quality of the issuer. Foreign investments involve greater risks than U.S. investments, and can decline significantly in response to adverse issuer, political, regulatory, market, and economic risks. Any fixed-income security sold or redeemed prior to maturity may be subject to loss.

Investing in foreign companies poses additional risks since political and economic events unique to a country or region may affect those markets and their issuers. In addition to such general international risks, the portfolio may also be exposed to currency fluctuation risks and emerging markets risks as described further below.

Changes in the value of foreign currencies compared to the U.S. dollar may affect (positively or negatively) the value of the portfolio's investments. Such currency movements may occur separately from, and/or in response to, events that do not otherwise affect the value of the security in the issuer's home country. Also, the value of the portfolio may be influenced by currency exchange control regulations. The currencies of emerging market countries may experience significant declines against the U.S. dollar, and devaluation may occur subsequent to investments in these currencies by the portfolio.

Foreign investments, especially investments in emerging markets, can be riskier and more volatile than investments in the U.S. and are considered speculative and subject to heightened risks in addition to the general risks of investing in non-U.S. securities. Also, inflation and rapid fluctuations in inflation rates have had, and may continue to have, negative effects on the economies and securities markets of certain emerging market countries.

A small-cap stock is a company with a market capitalization between $250 million to $2 billion. The precise figures used can vary among different brokerages, so this is a guide to their classification.

Definitions:

A tariff is a tax imposed by one country on the goods and services imported from another country to influence it, raise revenues, or protect competitive advantages.

The Tax Cuts and Jobs Act (TCJA) was a major overhaul of the tax code, signed into law by President Donald Trump in his first term on Jan. 1, 2018. The Senate passed TCJA on Dec. 2, 2017, by a party-line vote of 51 to 49. The House passed its version by a vote of 224 to 201. No House Democrats supported the bill, and 12 Republicans voted against it. The reform impacted taxpayers and business owners, particularly through tax cuts. Many of the tax reform benefits for individuals expire in 2025.

The acronym SALT refers to the state and local taxes deduction that taxpayers who itemize their federal tax returns are allowed to take. This deduction was unlimited until 2018, when it was capped at a maximum of $10,000 per year, or $5,000 for married people filing separately.

Inflation is a gradual loss of purchasing power, reflected in a broad rise in prices for goods and services over time.

The Trans-Pacific Partnership (TPP) was a proposed free trade agreement among 12 Pacific Rim economies.

When referring to being "overweight" or "underweight" relative to a market or asset class, RiverFront is referring to our current portfolios' weightings compared to the composite benchmarks for each portfolio. Asset class weighting discussion refers to our Advantage portfolios.

RiverFront Investment Group, LLC ("RiverFront"), is a registered investment adviser with the Securities and Exchange Commission. Registration as an investment adviser does not imply any level of skill or expertise. Any discussion of specific securities is provided for informational purposes only and should not be deemed as investment advice or a recommendation to buy or sell any individual security mentioned. RiverFront is affiliated with Robert W. Baird & Co. Incorporated ("Baird"), *member FINRA/SIPC, from its minority ownership interest in RiverFront. RiverFront is owned primarily by its employees through RiverFront Investment Holding Group, LLC, the holding company for RiverFront. Baird Financial Corporation (BFC) is a minority owner of RiverFront Investment Holding Group, LLC and therefore an indirect owner of RiverFront. BFC is the parent company of Robert W. Baird & Co. Incorporated, a registered broker/dealer and investment adviser.*