Timber Point Capital Management

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Bumpy Roads

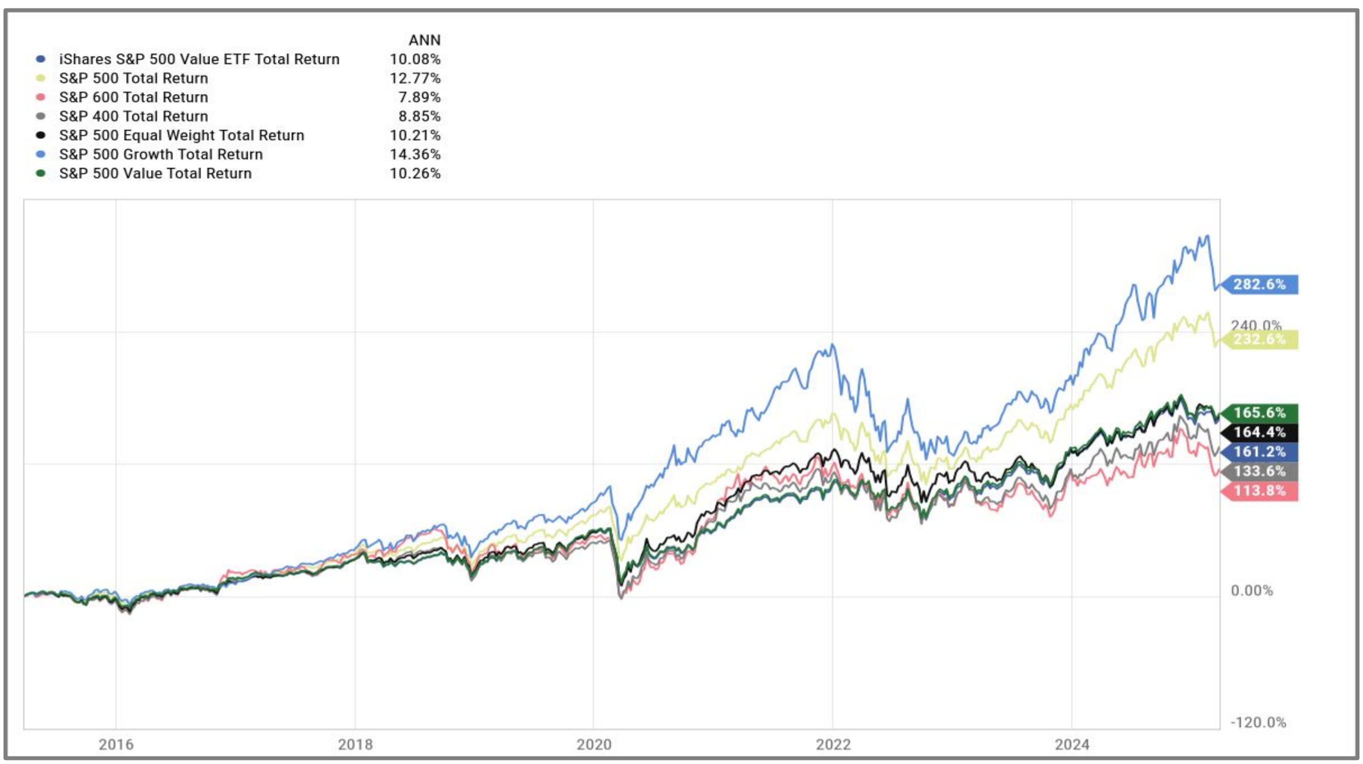
2Q 2025 Market Outlook

The new year began with a great deal of enthusiasm amongst the investor class. The election of Donald Trump was expected to unleash animal spirits in the economy and Wall Street strategists sharply increased 2025 US equity market targets. January was a bullish month, and the S&P 500 hit an all-time high on February 19th, only to quickly experience a bumpy 10% drawdown.

After an initial bout of post-election enthusiasm, the realities of Trump 2.0 began to kick in and investors started to evaluate the potential effect of tariffs, DOGE, budget reconciliation, Ukraine and other important policy initiatives. Given this firehose of Trump Administration proposals, the policy uncertainty variable increased and when uncertainty increases economic and market participants tend to retreat and pullback on risk.

Corrections are a normal part of investing, and market participants should not be overly surprised when they occur. In fact, 10% declines are somewhat routine, occurring once every 1 to 2 years with a recovery time that typically occurs within 6 months.

But what surprised investors most during the February-March decline was the darling stocks of the Magnificent Seven as well as other technology and AI growth companies got hit hardest, sharply exceeding the interim 10% decline in the broad index. For most of the last 10 years, large cap growth stocks led the overall market as the innovation driven by these companies led to sharp increases in earnings. Often, the large cap growth segment outperformed during down markets due to strong balance sheets and recession proof business models. Investing became an easy game by owning the largest and most recognizable market leaders.



Source: YCharts

So, what changed? Was it Trump tariffs and the market uncertainty or was it something much more straight forward? Trees don't grow to the sky and large cap growth stocks had gotten quite expensive over 2024 and their long-term prospects have diminished as earnings growth estimates have fallen. Additionally, given their outperformance, these growth darlings have reached epic proportions within indices and correspondingly their price action dominates index returns.

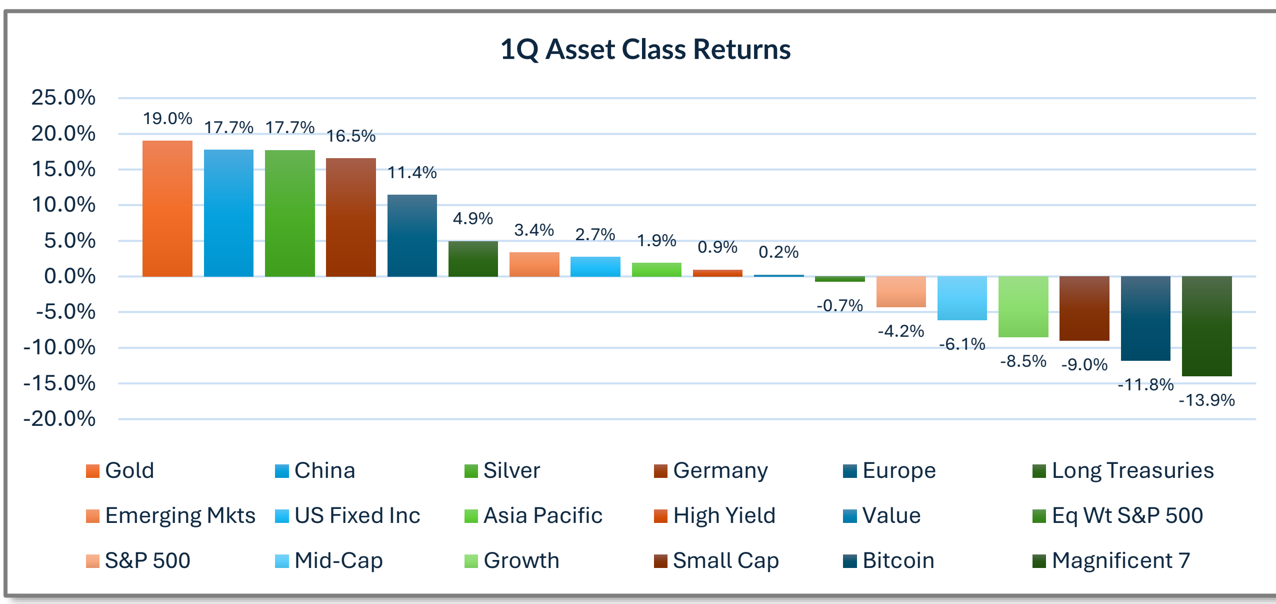
Price-to-Earnings of Magnificent 7 + Netflix

Name (S&P 500 Rank)	Current Market Value ($Bn)	Price-to-Earnings (Forward)	Estimated Long-Term Growth	Trailing 5-Year Earnings Growth*
Apple (1)	$3,259	27.8x	4.0%	10.8%
NVIDIA (2)	$2,824	26.0x	25.7%	91.7%
Microsoft (3)	$2,849	27.5x	12.3%	16.3%
Amazon (4)	$2,108	30.8x	4.0%	39.1%
Alphabet (5)	$2,037	18.4x	3.0%	24.1%
Meta Platforms (6)	$1,570	23.5x	10.3%	23.3%
Tesla (9)	$798	87.8x	14.4%	11.4%
Netflix (19)	$393	36.1x	23.0%	36.1%
Magnificent 7 + NFLX	*$15,839*	*26.7x*	*11.2%*	*34.3%*
S&P 500 ex. Mag 7+ NFLX	*$34,433*	*18.8x*	*10.7%*	*13.6%*
S&P 500	*$50,272*	*20.7x*	*10.8%*	*20.3%*

**Trailing 3-year where 5-year is not available*

Source: WisdomTree, FactSet, S&P. Estimated Long-Term Growth based on median analyst earnings growth estimates over the next 3 years. Growth rates as of 2/28/25. All other data as of 3/12/25. Aggregate metrics in italics shown as weighted averages. You cannot invest directly in an index.

Meanwhile, as US equities fell, other asset classes and investment types experienced a revival. Fixed income rallied over 2% as GDP growth estimates and inflation declined. European stocks, left for dead by many, posted double digit returns over the quarter and China rallied over 17% as various government stimulus measures have begun to have a positive impact. Gold and silver were also up nearly 20%.



Source: YCharts

Our overall takeaway from the first quarter is that a significant rise in policy uncertainty triggered a valuation adjustment among large-cap US growth stocks, pulling broader equity indices lower. That said, diversification benefits kicked in and well diversified portfolios generally performed better than the S&P 500, which was down about 4% for the quarter.

As always, valid questions and concerns exist and it's critical to assess the key variables to determine if the environment will be attractive for investors to take risk and where that risk will be best compensated.

2025 2Q Key Economic and Investment Drivers

Real Economic Growth	**Rising** **Stable** **Falling**	According to the Atlanta Fed, the economic growth trajectory in the US deteriorated dramatically over the last several months. We believe that while slowing, the US economy still can avoid a recession in 2025.
Inflation	**Rising** **Stable** **Falling**	Inflation improved throughout most of 2024, allowing for a pivot in monetary policy. Continued improvements may occur but will be more difficult going forward. The impact of pending tariffs could meaningfully sway the inflation trajectory.
Real Interest Rates	**Rising** **Stable** **Falling**	Real interest rates fell over the course of the quarter but remain near 10-year highs. A slowing economy and more accommodative monetary policy would result in further lower real rates.
US Dollar F/X Value	**Rising** **Stable** **Falling**	For many years the dollar has been the king currency among global competitors but trade uncertainty coupled with falling interest rates and a slowing economy may result in a weakening of the greenback.
Taxes and Regulations	**Rising** **Stable** **Falling**	The 2024 elections may be the catalyst for meaningful change in the tax and regulatory structure in the United States. The 2017 tax cuts are likely to be extended and DOGE has the potential to affect an unprecedented reduction in bureaucracy and red tape.
P/E Ratios	**Rising** **Stable** **Falling**	S&P 500 earnings growth is expected to modestly increase in 2025. US large cap growth remains at very full valuations which has resulted in a re-rating. Small caps, international and other market segments trade at meaningful discounts.
Fixed Income Risk Premiums	**Rising** **Stable** **Falling**	High yield spreads have widened out and represent a greater risk of economic slowdown and individual company stress. Although wider, we anticipate spreads remaining in a manageable range.
Volatility	**Rising** **Stable** **Falling**	On the back of Trump's tariff announcement, volatility spiked and will remain high until markets become comfortable that trade resolutions are developing.

Source: TPCM **Bullish Neutral Bearish**

Unmentioned above but critical in evaluating the forward-looking investment landscape is the Trump administration's ambitions regarding trade and tariffs. On April 2, the President gave a Rose Garden speech which outlined a sweeping set of tariffs against 90 different countries intended to level the global trade playing field in an effort to rebuild American industry and reduce reliance on imports. This move represents a significant escalation of Trump's new global trade policy that hopes to protect the US from unfair foreign competition while also generating federal revenue.

Specifically, Trump has proposed the following:

- A baseline 10% tariff on all imports from every country, effective April 5, 2005
- Additional tariffs on ~ 90 nations deemed “worst offenders” with significant trade imbalances effective on April 9, 2025
- A planned 25% tariff on all imported vehicles to be implemented in early April
- Additional sector specific tariff increases that will be announced at a later time

By major trading partner:

- China: Trump had already placed a 20% tariff at the beginning of his 2nd term; will now add additional 34% tariff bringing total to 54%; potential for additional 25% tariff if continue to buy Venezuelan oil
- Canada and Mexico: exempted from 10% baseline tariff and exemption applied to USMCA compliant goods; subject to previous tariffs of 25% on steel and aluminum imports and imported vehicles; a 25% tariff on specific goods until fentanyl and immigration flow curtailed; if fentanyl/immigration issues resolved, non-compliant USMCA goods face a 12% tariff
- Europe: 20% tariff on all imported goods from 27 member countries; 25% tariff on all imported vehicles

In calculating the tariffs charged by other countries the US has included not just the stated tariff rates of other countries but also added a calculation for foreign currency manipulation as well as other trade related barriers that added to the cost of selling US exports. While discounting this total by 50% to arrive at the new tariff rate, the net effect was that the tariffs proposed were much higher than what most had expected.

The broader economic outlook remains uncertain, with rising concerns that trade disruptions could lead to a significant US slowdown. While European markets have shown more resilience, historical patterns indicate that a downturn in the US could ultimately weigh on global growth, particularly in export-dependent economies like Germany, Japan and the UK. Investors remain cautious about the risk of stagflation, given the Federal Reserve's uncertain capacity to offset the impact of trade tensions through monetary policy. However, we believe that Trump’s trade and tariff policies will remain flexible, leaving room to prevent a full-scale trade war.

From our vantage point the end game is still being played out as it appears the Trump administration has left themselves a very narrow window in which to further negotiate rates lower with specific countries until the April 9th deadline arrives. While there will undoubtedly be tough public talk from all countries, there will also likely be behind the scene discussions on how to move forward now that the US framework has been announced. Already we have seen that Israel has agreed to remove tariffs on US imports, Vietnam is in discussions to lower tariffs and India is in discussions to lower duties imposed on US goods. We would expect additional conversations will take place at a frenetic pace.

In addition, Trump's threat of tariffs to this point has resulted in an unprecedented number of announcements of investment into the US by foreign and US companies. While some of this may have occurred without the tariff threat, there is little doubt that many companies have chosen to invest directly in the US rather than Mexico or Canada or elsewhere to fully avoid future tariffs. Trump's ability to bring investment into the US is a direct repudiation of the "globalist" view on trade which shipped jobs overseas in return for much cheaper goods. Below is a list of recent announcements.

Over $3 Trillion in Investment Commitments since Inauguration

Companies

•**Apple**: Pledged $500 billion for U.S.-based investments, announced in early 2025. This includes initiatives in AI infrastructure and manufacturing, though specifics on timelines and allocation remain broad.
•**NVIDIA**: Committed over $100 billion for U.S.-based manufacturing operations over the next four years, announced in March 2025, focusing on chipmaking and AI infrastructure.
•**Taiwan Semiconductor Manufacturing Company (TSMC)**: Announced a $100 billion investment in Arizona for semiconductor fabrication facilities on March 3, 2025, adding to a prior commitment, bringing their total U.S. investment to $165 billion.
•**Johnson & Johnson**: Pledged $55 billion in March 2025 for a high-tech facility in North Carolina, aimed at manufacturing advanced medicines and creating U.S. jobs.
•**Hyundai**: Committed $20 billion, announced in March 2025, including a $5 billion steel plant in Louisiana expected to create 1,500 jobs.
•**SoftBank**: Announced a $100 billion investment over four years in December 2024 (pre-inauguration but reinforced post-January 20, 2025), targeting AI and related infrastructure, with a goal of creating 100,000 jobs.
•**Stargate (SoftBank, OpenAI, Oracle collaboration):** Pledged $500 billion over four years for AI infrastructure, announced in early 2025, often cited alongside Trump's economic policies.
•**Nippon Steel:** Committed $14.1 billion, noted in February 2025, though tied to a broader acquisition context that predates the administration.
•**DAMAC** (Hussain Sajwani): Announced $40 billion in early 2025, though some reports list a lower figure of $20 billion, reflecting potential variability in scope.

Countries

•**United Arab Emirates (UAE)**: Pledged $1.4 trillion over 10 years, announced in early 2025, to sustain investments in AI infrastructure, semiconductors, energy, and manufacturing.
•**Saudi Arabia**: Committed $600 billion, announced in early 2025, as part of a broader economic partnership with the U.S., often linked to Trump's "America First" agenda.

Source: Grok

We believe these capital investments, coupled with the likely extension of tax cuts from the first Trump administration, will sustain economic momentum and help stave off a recession. However, recent tariff announcements introduce a significant new risk for investors. Recession? Inflation? Stagflation? The landscape remains uncertain, but there is a pathway to policy success.

With Trump, nothing is ever static. As he wrote in *The Art of the Deal*, "If you're going to be thinking anyway, you might as well think big." His tariff strategy and other proposals clearly reflect that mindset. The success of fiscal policy will hinge on the timing and execution not just of tariffs but also tax cut extensions, regulatory reform, and DOGE initiatives. Thinking big indeed but with big thoughts come big responsibilities. Can he pull it all off without throwing markets into greater volatility?

So far, investing conditions have certainly been very challenging. Investors must take an objective approach to identify opportunities aligned with their goals. Volatility is the price of excess returns. As such, our forward-looking investment strategy considers policy developments, relative valuations, and growth potential across asset classes.

2025 2Q Asset Class and Sector Probabilities

Major Market Asset Class	Likelihood of Outperformance
Bonds outperform Cash	62.5
Equities outperform Bonds	55.0
Non-Traditional outperforms Equities	62.5
Non-Traditional outperforms Bonds	54.4
Europe outperforms the US	50.5
Asia outperforms the US	46.5
EM outperforms the US	53.0
Small Cap outperforms Large Cap	47.0
Mid Cap outperforms Large cap	55.0
Value outperforms Growth	48.0
Credit outperforms Government bonds	51.0

Sectors v Market	Likelihood of Outperformance
Discretionary	44.4
Energy	35.9
Financials	61.4
Health Care	62.4
Industrials	38.3
Info Tech	63.9
Materials	54.5
Real Estate	54.1
Staples	40.4
Communications	52.9
Utilities	41.8

Source: TPCM Bullish Neutral Bearish

Despite everything, we do not believe this is the time to significantly reduce risk. While policy and related economic uncertainty remains high, much of those risks have already been priced in during this recent correction. Sentiment is now deeply depressed, hovering near the lows of March 2009. More importantly, portfolio positioning and leverage are at very defensive levels.

Markets have clearly adopted a “shoot first, ask questions later” mentality since Trump’s tariff announcement last week. The focus has largely been on potential downsides, with significant time and energy spent analyzing what could go wrong. But at current levels, it may be worth taking a more balanced view—one that weighs both risk and opportunity. Just as markets quickly priced in the economic threats of the tariff policy, they could just as rapidly respond to any signs of easing tensions or movement toward a resolution.

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