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PEAK CAPITAL MANAGEMENT

The Survey Says...

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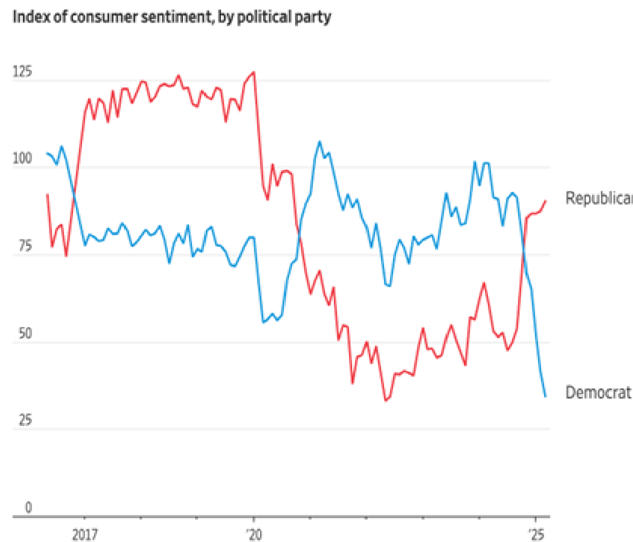
The most recent economic data suggests the economy could be headed for a hard landing sooner rather than later. The headline number from the University of Michigan Consumer Sentiment index in April plunged from 57 to 52 suggesting consumers are more uncertain about future economic activity. The Future Expectations part of the survey has dropped 32% since the January reading to the lowest level since the 1990 recession. Alarmingly, consumers surveyed expect prices to rise 6.5% over the next 12 months, an increase over the 5% expected rise in prices from the March survey.

The story the headline number does not tell is how much a respondent's political view is influencing the data. Democrats responding to the survey posted the lowest sentiment number ever at just 34 while Republicans as a group were at 90. Not only is the political divide in our country seemingly unprecedented, how you feel about the future of the economy is largely driven by your political view.



Not all data regarding the economy is concerning. The Bureau of Labor Statistics (BLS) Household Employment survey shows unemployment remaining steady 4.2%, in line with where it has been since May 2024. The Conference Board survey on Consumer Confidence has possibly the most interesting data as of March 2025. The broad survey tumbled over 8% in March to 92.9 while the Expectations index fell an astonishing 15% to 65.2, the lowest level in 12 years, and where anything below 80 has historically suggested a recession within 12 months. What surprised me about the data is the difference in confidence based on your age. Respondents over 55 years of age were overwhelmingly negative about the economy while those between 35 and 55 were mostly unchanged. Those below age 35 actually saw an increase in confidence from the prior month suggesting the younger population is more positive about the direction of the economy. Income levels were also a stark difference with those making less than $125,000 per year seeing large decrease in confidence while those making over that figure saw an increase in confidence. This was surprising given the market volatility as higher income individuals hold the vast majority of stock market investments.

> "The most recent economic data suggests the economy could be headed for a hard landing sooner rather than later."

The business data, while mixed, was much more upbeat in the last month using the Purchasing Managers Index (PMI) as a guide. US Services PMI rose 6% to 54, the highest reading of 2025, while the Composite index (includes manufacturing) rose to 53.5, also the highest in 2025. Both indices remain above the important 50 threshold that suggest economic expansion rather than contraction.

I believe the volatility in the sentiment and confidence data is driven by Trump's negotiating style that many in the US and abroad are still adjusting to. Statements are often made and actions taken that seem more likely to be framing negotiations than actual policy that is likely to be implemented. The idea of "Free Trade" is often discussed but tends to be very subtle. For example, even with Free Trade agreements with Canada, US farmers pay tariffs on many agricultural products exported to Canada. The US consumer market is the largest in the world and every country wants to export to the US. Trump is trying to provide a more level playing field but his style in doing so is proving to be incredibly disruptive to the markets and economic expectations.

There is real-time economic data suggesting a contraction is imminent. Shipping and cargo data is a leading indicator of demand that is critical to GDP calculations. The trade war with China is having an immediate impact on container shipments from China to the US. Container bookings from China have fallen 60% in just the last two weeks and many of the ships are carrying only 50% of their capacity. Trucking volumes have fallen dramatically and are near COVID-era lows today. A scarcity of products in stores will lead to higher prices as consumers have no choice but to make purchases on many products. The tariff's may create a more level playing field in the future but in the short-term they are likely to have a recessionary impact on the economy.

The recent market volatility may be a sign of what to expect over the next 3-6 months. We are still in the early stages of corporate earnings being guided lower and that is likely to impact valuations and the price investors are willing to pay for stocks. The transformative impact of AI on the economy and markets has to be balanced with the likelihood of a recession where the depth is very uncertain. Keeping hedges on portfolios appears to be sensible as the markets could remain in a "risk-off" environment for the foreseeable future.

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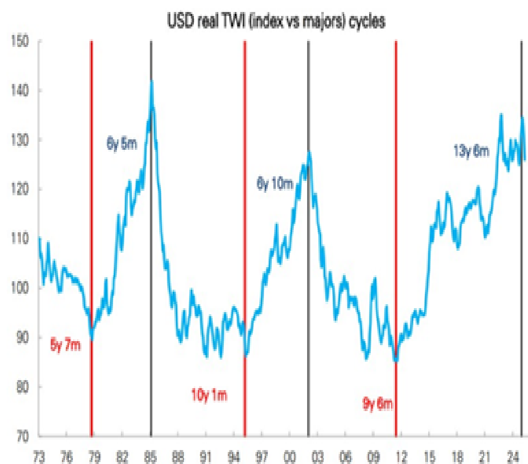
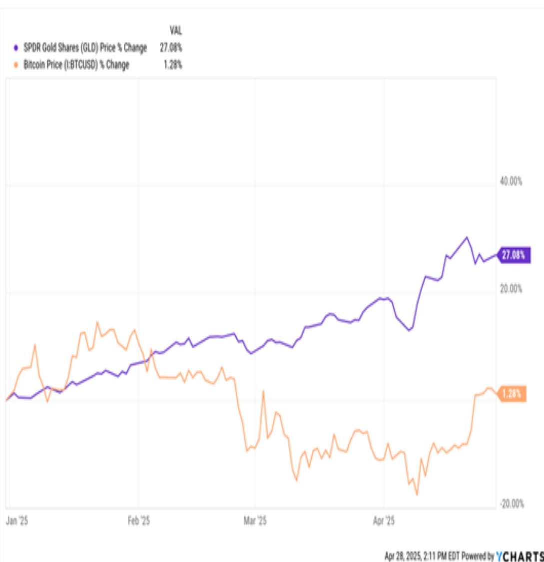
Regime Change for the USD?



The US dollar has essentially traded in just 6 cycles over the last 50 years with the most recent bull market cycle appearing to come to an end after 13 long years. The rise and fall of the US dollar has typically coincided with global events such as the Asian currency crisis of the late 1990's, the tech bubble crash of the 2000's or the Euro zone crisis that began in 2012. While there may not be another currency to rival the US for reserve currency status, in a world of digital currencies it has become less important. The volatility in US trade policy since Trump was elected President has made the US a less attractive place to invest according to many. It seems likely the US dollar is entering an intermediate to long-term decline against the Euro, Yen and Pound.

- There has been a recent decoupling of US interest rates and the value of the USD. Higher rates have historically corresponded with dollar inflows that appears to have ended.
- While tariff's are intended to address the massive US trade deficit, the fact remains that the twin deficits of Budget and Trade are weighing on the value of the greenback.
- There are economists calling for a significant weakening of the US dollar in order to make US goods more affordable as exports and to help in monetizing US debt obligations.

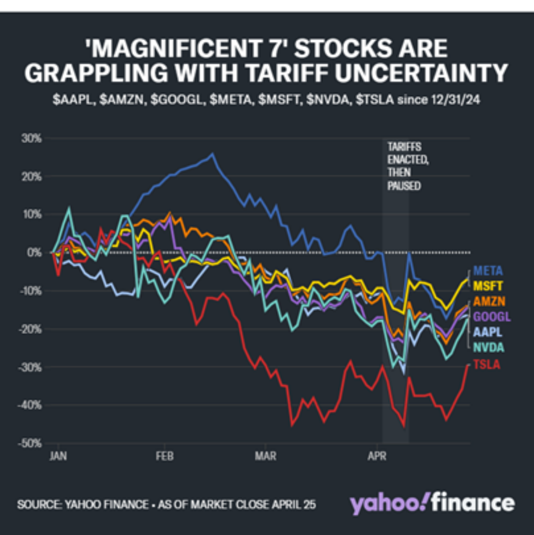
Gold vs. Bitcoin



Amid the backdrop of heightened equity volatility around tariffs and a potential recession, two potential hedges have delivered positive absolute returns and negatively correlated exposure to stocks. As the chart illustrates, gold has surged by roughly 30% for the year as investors have flocked to the precious metal over concerns about inflation and a weaker dollar. Meanwhile, bitcoin has surged roughly 10% since the tariff announcements in early April after declining by roughly -8% to start the year. Both assets have outpaced the S&P 500 year-to-date.

- So far gold has won the race against bitcoin over an incredibly volatile equity environment. From a diversification standpoint, gold has exhibited a correlation to the S&P 500 of roughly 0.20 for the year which suggests a weak relationship to movements in the equity markets. Likewise, the correlation of bitcoin to the S&P 500 is essentially zero for the year.
- Moves in bitcoin were much more pronounced compared to gold, with 13 days of gains or losses of 5% or more. Gold, meanwhile, exhibited roughly half the volatility of the S&P 500. Combined with its return, the precious metal provided relatively attractive risk-adjusted performance for the year.

Markets Brace for Key Data



Markets enter a pivotal week as investor optimism faces a test from critical economic data and a wave of corporate earnings. Stocks rebounded sharply last week after President Trump signaled a softer stance on tariffs and reaffirmed support for Fed Chair Jerome Powell, easing concerns over central bank independence and trade. The S&P 500 surged 4.5%, led by tech gains, while attention now shifts to key releases including Q1 GDP (expected at just 0.1%), core PCE inflation, and the April jobs report. Big Tech earnings from Apple, Amazon, Microsoft, and Meta may further influence sentiment as investors look for clues on resilience in the face of tariff uncertainty and AI competition.

- Trump's pivot on tariffs and Fed independence helped reverse a nearly 1,000-point drop in the Dow, contributing to the S&P 500's 4.5% weekly gain and Nasdaq's 6.6% surge.
- Economists forecast Q1 GDP at just 0.1%, the slowest since 2022, as tariff effects begin to weigh on output.
- Large-cap tech stocks continue to drive gains, but upcoming earnings will be crucial to sustaining momentum. Microsoft and Meta are set to report on the 30th, while Apple and Amazon report the following day.

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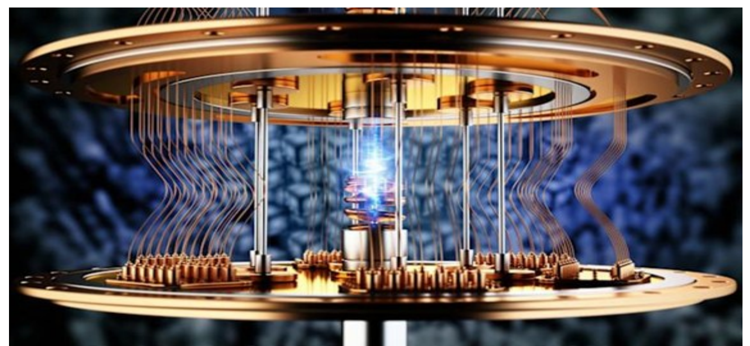
Quinn VandeKoppel

Macro View – Trade Tensions Escalate

Treasury Secretary Scott Bessent stated Monday that China must take responsibility for de-escalating trade tensions, highlighting that China's exports to the U.S. far outweigh U.S. exports to China, making current tariffs of up to 145% unsustainable. His remarks follow President Donald Trump's April 2 announcement of broad-based global tariffs, later adjusted to a 10% across-the-board rate with a 90-day pause on harsher measures. Bessent noted progress in negotiations, pointing to India as likely the first new trade agreement. He also said European nations are "in a panic" over the euro's 10% rise against the U.S. dollar and predicted the European Central Bank would cut rates to weaken the currency. Despite mixed signals from the White House on China talks, Bessent stressed that negotiations would not be conducted through the media.

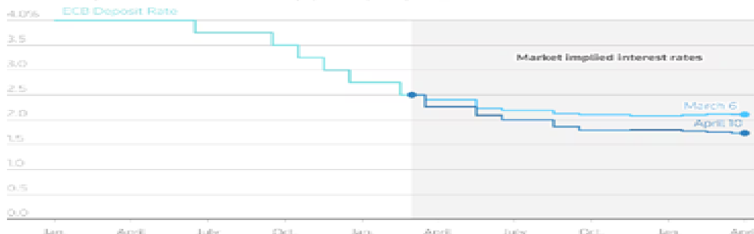
Taking Stock – Quantum Race Urgency

Microsoft President Brad Smith urged the U.S. government to prioritize quantum computing research, warning that China could soon match or surpass American capabilities, threatening economic competitiveness and national security. Smith called for renewed funding through the National Quantum Initiative Act, expanded DARPA programs, strengthened education pipelines, and incentives for building a U.S.-based quantum supply chain. Quantum computers, capable of solving complex problems beyond traditional computers' reach, could also break current encryption methods, posing severe security risks. Microsoft recently unveiled its Majorana chip with eight qubits, aiming for a long-term goal of one million. Despite recent breakthroughs by Microsoft and Google, experts caution that commercially useful quantum computers are still decades away. Smith emphasized that failing to maintain U.S. leadership in quantum technology could have serious economic and security consequences.



Fixed Income – German Boost vs. Tariffs

Higher infrastructure spending in Germany is expected to boost Europe's economy but not enough to offset the drag from U.S. tariffs, according to Alfred Kammer, head of the IMF's European department. Last week, the IMF cut euro area growth forecasts by 0.2 percentage points for both 2025 and 2026, citing tariff-driven trade tensions. Germany's new €500 billion infrastructure and climate fund will support growth, but optimism has been dampened by the broader global slowdown. ECB policymakers indicated tariffs could further reduce inflation but acknowledged rising uncertainty. The IMF recommends the ECB cut interest rates just once more this summer, by 25 basis points, then pause unless major shocks occur. The ECB's key deposit rate currently sits at 2.25% after seven cuts since June 2024. Markets, however, are pricing in expectations for two additional cuts this year.



Technical – Relief Bounce

Following President Trump's "Liberation Day" tariff announcement in early April, the stock market experienced a sharp and immediate decline as investors reacted to the prospect of heightened trade tensions. The S&P 500 dropped over 12% across the five trading sessions that followed, including a steep 6.65% plunge on April 3rd—one of the index's worst single-day losses in recent years. The selloff brought the S&P 500 dangerously close to bear market territory, down more than 20% from its most recent peak, underscoring the market's sensitivity to aggressive shifts in trade policy and the perceived risk to global economic stability. However, since the S&P 500 hit its low for the year on April 7th, the large cap index has since rallied more than 15% and now currently sits in a wide range where risk vs reward remains more of a tossup in the near term.

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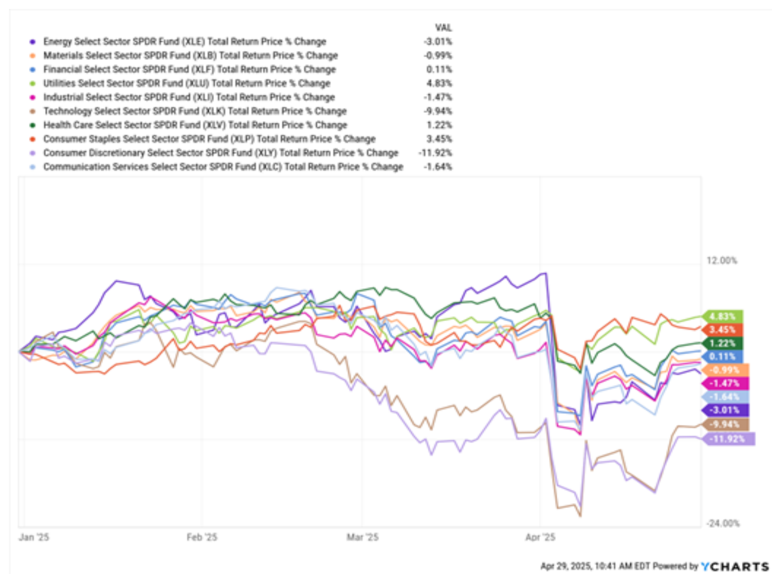
Performance Review

Clint Pekrul, CFA

Investors have been on a rollercoaster ride this year as market volatility has reached elevated levels. The CBOE VIX Index, the so-called fear gauge, has traded at an average level of 23 since Trump's election compared to the long-run average of 15. The S&P 500 Index slid into correction territory and long-term interest rates traded erratically on Trump's tariff announcement. Meanwhile, the USD has weakened considerably. It's helpful to evaluate performance by asset class for the year to decipher the relative winners and losers.

U.S. Equity Sectors



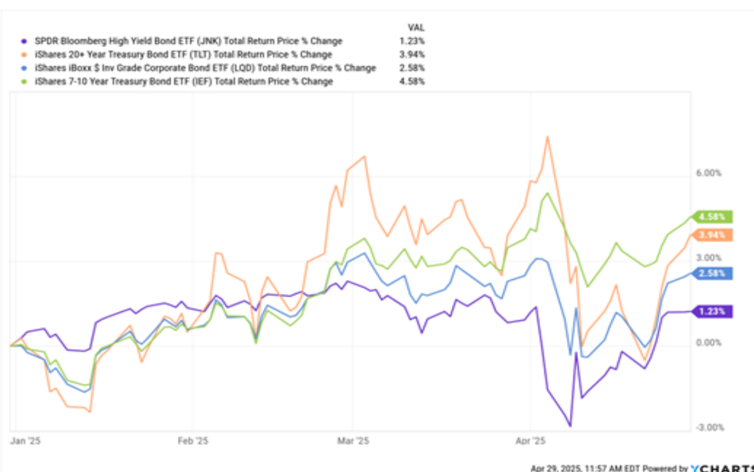
Not surprisingly, the technology and consumer discretionary sectors are the weakest performers for the year. From a valuation standpoint alone, technology stocks collectively were arguably overvalued entering 2025. The markets had priced considerable growth prospects on the back of AI capital investment. Perhaps the market went too far and is now clawing back some of the gains experienced over the past few years (i.e. profit taking amid heightened economic uncertainty). However, the pullback does not necessarily negate the long-term growth prospects from AI innovation.

With the prospect of a looming recession, consumer discretionary stocks have the weakest relative returns for the year (12%). In a pattern typical for the sector, when the market anticipates a scenario of weak to negative GDP growth and rising unemployment, discretionary stocks are generally adversely affected. If we do enter a recession, the pullback can provide an attractive buying opportunity for investors who are willing to wait for an eventual recovery.

The relative outperformance for utilities and consumer staples is also not surprising. For the year, the utility sector has delivered positive absolute returns (5%) and the strongest relative performance. Perhaps one reason for the strong returns is the electricity demand for AI development, which could be somewhat immune to tariffs. Historically, the utility sector has been considered "recession proof" although there is no guarantee the sector will not succumb to an economic slowdown.

As the name suggests, consumer staple stocks provide everyday essential items for consumers, and are considered non-cyclical. Consequently, the sector tends to outperform when recessionary fears are on the rise. However, this sector is not necessarily immune to tariffs as these companies face higher import costs. Ultimately, though, these stocks can potentially pass along these higher costs to the consumer.

US Fixed Income



Sectors of the U.S. fixed income market are generally higher for the year. Credit conditions remain favorable for now, but conditions could deteriorate if the economy slows. Option adjusted spreads (OAS) remain tight relative to historical averages. The high-yield market was a relative underperformer across the asset class, although still higher on an absolute basis. Should OAS widen, high yield could present an attractive entry point for longer-term investors. Investment grade corporate bonds modestly outpaced high yield bonds for the year.

Prior to the April 2nd tariff announcement, the ten-year Treasury yield had fallen to just under 4%. However, conditions reversed quickly due to the uncertain outcome of a prolonged trade war whereby Treasuries might not be viewed as a safe haven asset.

Investors using Treasuries as a potential hedge to equity volatility should consider the stagflation scenario. For example, tariffs could be passed through to the consumer which could lead to higher overall prices (i.e. inflation) coupled with a recession. Consequently, the Federal Reserve would be limited in its ability to lower interest rates and thus curtail a bond rally to offset equity losses.

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Q: When do you expect the National Debt to dominate economic headlines?

Both the deficit and the debt are grabbing a lot of headlines right now, especially in light of the cost-cutting efforts of DOGE. What is likely inferred by the question is when will the debt level in the US become unsustainable and directly impact the ability for the economy to continue to expand. One of the more comprehensive studies on sustainable debt-to-GDP levels was done by the Wharton School at Penn with their Budget Model. Their research suggests that a debt level of 200% of GDP is unsustainable and a country would likely have to default in some respect. Additionally, Reinhart and Rogoff's 2010 research demonstrates that economic growth is negatively impacted when debt-to-GDP levels exceed 90%. High debt levels increase the risk of a country entering a death spiral in financing their debt where debt issuance drives interest rates higher and causes servicing the debt to increase exponentially. This leads to a default such as Argentina and many African countries have experienced.

IMF data currently shows the US debt-to-GDP at 118%, Italy at 135%, France at 110% and the UK at 101%. China's data is questionable but reports at 85% while Australia is only at 43%. The outlier is clearly Japan at 249% debt-to-GDP and their debt levels have exceeded 200% since 2010 without an economic crisis unfolding. It likely explains why Japan's annual GDP growth rate have averaged - 0.1% per year since 2020 and just +0.8% per year since 2010.

I think it's fair to say that since COVID and the subsequent explosion in federal spending, the issue of the national debt, or rather its size relative to total economic output, is discussed more frequently than in the years leading up to the pandemic. What is driving the debate, to some degree, are the fiscal policies that have led to trillions in spending at a time when the U.S. economy was expanding and at full employment. Some will argue that this spending was necessary to avoid a total stall of the U.S. economy in 2020. However, I think the more pertinent observation is that Washington went too far too fast for a simple reason – interest rates were zero.

Fast forward to 2025 and the economic situation looks much different. It costs more to borrow today than it did five years ago as the Federal Reserve raised interest rates to curb inflation in 2022. What is most concerning is the cost to finance the debt burden. According to the CBO, total interest payments were $476 billion in 2022 but will jump to $952 billion by the end of 2025. As a share of federal revenues, federal interest payments would rise to 18.4 percent by the end of 2025, exceeding the previous high set in 1991. They would reach 22.2 percent by 2035. I think we're on an unsustainable path, considering we have an aging population with declining birth rates. Likewise, because of tariff policy, the Federal Reserve might not be able to lower rates should we enter a recession, which would make the problem worse.

Q: Is the labor market starting to show signs of stress?

There are many signs that suggest the tight labor conditions are ending and unemployment may be starting to rise. The labor participation rate still has not returned to pre-COVID levels and is hovering around 62% compared to 67% in 2000. Recent college graduates are really struggling with an unemployment rate of 5.8% but an underemployment rate of 41%. This represents recent college grads who can only find part-time work or work not related to their degrees such as barista's, bartenders, or gig delivery jobs. Announced layoffs are also making job hunting more challenging and it is not just the Federal government eliminating jobs. Large companies like Starbucks, Chevron, Intel and JP Morgan all announced significant layoffs. The QUITs rate, which shows the percentage of employee willing to resign from their current position, has fallen by 35% since 2022 and is below 2%. This suggests even workers who are not satisfied with their current role are staying put as finding a replacement position has become more challenging. One last data point is jobless claims reported by the Dept of Labor. Initial Jobless claims have remained steady over the last 2 years, averaging 220,000 per week. Continuing claims, counting those who remain on unemployment unable to find a job, have risen during that period from 1.4 million to over 1.8 million. The labor market remains resilient with 4.2% unemployment but there are signs it is weakening.

We successfully brought down the unemployment rate from 15% in April 2020 and have been at full employment (less than 5%) since mid-2021. According to the Bureau of Labor Statistics, the unemployment rate hit 3.4% in April 2023 but has increased to 4.2% as of March 2025. While we are still at full employment, we have been trending closer to 5%. What is noteworthy is how tariff policy, or its lack of transparency, could impact small businesses. According to the Bureau of Labor Statistics, small businesses, which employ 500 or less, represent roughly half the workforce, or 60 million people. Yet small businesses might be ill equipped to handle new tariff policies, which could translate into lower margins and ultimately layoffs.

For small businesses that import, particularly from China, the new tariff policy could strain cash flows as expenses would immediately rise. One option would be for owners to pass along the higher costs to consumers as a consumption tax. But for small businesses this might not be an option as pricing power could be limited and the goods they import from overseas aren't readily available in the US. Owners would have to absorb some of the costs but would ultimately likely layoff employees. Roughly two-thirds of small-to-medium sized businesses rely on imports, of which 40% come from China. So, the tariffs could have an immediate adverse impact on the employment rate as owners adapt to new policy.

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