Newsletter

MCS Family Wealth Advisors

Managing Risk to Increase Wealth®

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2025 Second Quarter Newsletter and Outlook

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> *"Democracy is the theory that the common people know what they want and deserve to get it good and hard."*
>
> — H.L. Mencken

In the last quarter, the stock market was down on tariff uncertainty. This quarter, the stock market has shaken off the tariff threats, ending up 6.2%. Bonds, meanwhile, were up 4.02% through June 30. Does it matter that the world is being upended (to your delight or horror depending on your point of view) by the new administration and AI technology, developments which have significant consequences, some of which will be unforeseen and unintended?

Trade & Immigration Policies: Inflation and Market Implications

This quarter's report is a bit of an experiment. Given the complexities of the current investment environment, I decided to use AI to assist me in sorting it out. I was interested in the likely economic impact of the Trump administration's tariff policies, which admittedly are moving targets, and its immigration policy. Although these issues are studied by economists, they are rarely significant enough to be on Wall Street's radar, until now.

Overall, tariffs and inflation are positively correlated, meaning that they move in the same direction. The same goes for immigration and economic growth. Trump's policies are to increase tariffs (implying higher inflation) and decrease immigration (implying slower economic growth), a recipe for potential stagflation.

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Tariffs and Consumer Prices

Table 1

Where We Are Now

Country / Product	Headline Tariff Announced	What Partners Thought Was Coming
Canada (all goods)	**35 %** blanket duty	Ottawa expected to stay at baseline 10 %
Copper & semi-finished copper	50 %	N/A - Unexpected
Vietnam (all goods)*	**20 %**, plus 40 % on goods deemed "trans-shipped"	Vietnamese negotiators believed **~11 %** was the handshake number during June talks
Baseline "reciprocal" tariff (all other imports)	**10 %** (unchanged)	N/A, Executive Order 14257

These rates all start **August 1**, subject to ongoing trade litigation.

Walmart (WMT) has already announced price increases due to tariffs. CEO Doug McMillon said in May, on the company's first quarter earnings call, that the giant retailer was trying its "best to keep our prices as low as possible. But given the magnitude of the tariffs… we aren't able to absorb all the pressure given the reality of narrow retail margins. The higher tariffs will result in higher prices."

If you are a student of economic history, you may recall that the Smoot-Hawley Tariff Act of 1930 was *'intended to bolster domestic employment and manufacturing, the tariffs instead deepened the Depression because the U.S.'s trading partners retaliated with tariffs of their own, leading to U.S. exports and global trade plummeting.'*[1] So while initial tariffs increase prices, in an escalating retaliation scenario, the tariff war price increases discourage buying thus undermine economic growth.

Given the unconventional nature of trade negotiations, it is difficult to pin down what future tariffs might be and, consequently, their impact on inflation and the economy. The bias is for higher inflation, but the magnitude in the short and longer term is difficult to forecast. This is why the Fed, which has a mandate to control inflation, has taken a wait-and-see approach. (More about this in the last section.)

Table 2

The Vietnam Experience

What Vietnam's "11 % → 20 %" Surprise Tells Us About Trump's Tactics

Feature of the Move	Practical Effect	Strategic Upside for the White House	Strategic Downside / Risk
Last-minute rate hike (Vietnam expected ~11%, got 20%)	Keeps trading partners off-balance; signals "take-it-or-leave-it" leverage.	May force faster concessions from smaller countries that fear worse terms later.	Undermines trust, making allies hesitant to invest or sign detailed deals (Hanoi now pushing for written guarantees).
Adds a "trans-shipment" clause (40% if inputs trace back to China)	Creates wide discretion: U.S. Customs can punish Chinese content routed through third countries.	Discourages duty-dodging; fits narrative of closing loopholes.	Raises compliance costs; foreign investors may rethink Vietnam as a China-plus base if rules are vague.
Public announcement before legal text	Controls the news cycle and frames the narrative ("Vietnam pays, U.S. sells at zero tariff").	Domestic political win—sounds tough at rallies.	Markets, suppliers and even U.S. importers lack clarity; raises supply-chain risk premia.
Pattern matches earlier moves (threaten 46%, settle at 20%)	Shows willingness to "walk back" from extremes, claiming a victory.	Reinforces image of hard bargaining that extracts mid-range deals.	Partners may adopt a wait-it-out strategy—assume initial threats won't stick.

What does the table above tell us?

- **Unpredictability is the point.** The White House starts with a high tariff number, keeps revising it in public, and often announces details before the formal text.
- **Price in headline risk.** Stock markets are reacting less to first headlines but still jump on the final rate reveal (e.g. Vietnamese apparel shares – 6 % on 10 July).
- **Legal wording matters.** Open-ended clauses (like the 40% "trans-shipment" penalty) create uncertainty and decrease bond prices (the added yield investors want for long term bond risks) even if the revised tariff rate looks lower.

Immigration Policy and Wages

In the US today, about 19% of workers are immigrants. Industries such as construction, farming, hospitality, and elder care rely heavily on foreign-born workers. The Trump Administration has promised "the largest deportation operation in US history." Moody's Analytics estimates that removing 8 million undocumented workers would cut real GDP by about two-and-a-half percent by 2027, and it would also push core inflation up by 0.4% through increased wage growth due to a scarcity of workers. But what is the likelihood of this happening?

The tables below are AI summaries of the probabilities and their origins.

Table 3

Current Immigration Enforcement Probabilities 'Experts' Assign

Immigration Path	Rough Odds	Impact on Wages and Prices
Normal enforcement continues	45 %	Little change
1–2 million removals	25 %	Small wage-push
8 million removals	**15 %**	**Noticeable wage-driven inflation**
Courts or Congress block mass removals	15 %	None

Bottom line: fewer immigrant workers creates a tighter labor market and higher service prices, especially in sectors that already struggle to hire.

Table 4

Sources of Immigration Probabilities (cited by AI)

Scenario	Status-Quo Enforcement	Deportations (1–2 Million)	Mass Deportation (≈8 Million)	Blocked in Courts / Congress
Primary evidence	CBO **baseline** assumes no change in law or funding—"net immigration roughly stable." Xinhua	Dallas Fed staff paper models a **moderate-tightening path** (≈ 2 ½ million fewer unauthorized workers through 2028). Federal Reserve Bank of Dallas	Moody's Analytics "mass-deportation" campaign scenario (March 2024) removes the entire unauthorized work-force and sees GDP – 2½ % by 2027. Xinhua	Federal courts have already blocked several birth-right and asylum rules; House Democrats and some GOP moderates have vowed to deny funding for large-scale removals. American Immigration Council
Political / legal filters we applied	~50% chance Congress simply extends current DHS budget with no new deportation money.	Requires: extra ICE funding and no nationwide injunctions—judged "possible but not certain."	Requires both Houses to approve $10 billion or more per year for ICE beds and courts to allow sweeps—significant hurdles.	Mirrors past pattern: courts stall, or Congress starves program
Scenario's implied odds[2]	**45 %**	**25 %**	**15 %**	**15 %**

Source: OpenAi. (2025). ChatGPT o3 (April 16, 2025 version) [Reasoning large language model].

Note: The odds will change. A single court ruling or funding deal can increase or decrease the odds by 10–15 percentage points overnight—watch the September budget process and any nationwide injunctions.

One More Thing About Immigration

Republican business owners have pressured the Trump Administration to create “carve-outs” for specific industries that are highly dependent on immigrant labor. Trump did **carve out, pause, then re-activate enforcement** in hospitality and agriculture, and is now pitching a narrow visa fix instead of broad exemptions

Table 5

Trump’s Temporary “carve-outs” for Hospitality, Farming, and Food Service

Date (2025)	Event	What changed
12 June	DHS e-mail instructs ICE to **pause work-site raids** at hotels, farms, restaurants, meat-packing plants	Enforcement frozen for labor-short industries
16 June	Senior officials **reverse the pause** after backlash from hard-liners	Field offices said raids are back on across all sectors
18 June	White House briefly reiterates the pause, then rescinds it within 48 hours	Confusion inside ICE; businesses left guessing
11 July	New announcement: **fast-track visa channel** for seasonal farm and hotel workers (must apply abroad)	Promises relief without legalizing current undocumented staff

What the Stop-Start Strategy Means

Feature of the Tactic	Possible Upside for the White House	Likely Downside for Businesses and Markets
Surprise pauses and reversals	Keeps political base energized while signaling “flexibility” to key industries	Raises operating uncertainty; firms postpone hiring and investment
Selective concessions (fast-track visas)	Lets administration claim it is “solving shortages without amnesty”	Visa rules still untested; does not protect current undocumented staff — labor gaps remain
Public announcements before written guidance	Controls headlines and bargaining narrative	HR and legal teams have no firm rules to rely on; increases compliance risk
Targeted raids after carve-outs	Sends message that enforcement will hit non-cooperative sectors hardest	Perceived favoritism may invite legal challenges on equal-protection grounds
Negotiation by whiplash (11% deal → 20% tariff on Vietnam; pause → resume raids)	Creates leverage—partners may settle quickly to avoid worse terms	Trading partners and domestic industries learn to “wait it out,” which can prolong stalemate and weigh on growth

Economic implications of the "start-stop" strategy

The start-stop nature of the carve-out policies will keep wage and price pressure elevated. Fast-track visas help only future seasonal hires; they do not offset the hit from stepped-up raids on existing staff. **Business costs will rise,** as companies will have to budget for (a) higher legal/compliance outlays and (b) potential production stoppages if raids resume. Finally, **policy credibility will erode** because of repeated flip-flops pressure bond and stock prices: investors demand extra compensation for rules that can change overnight.

What Tariff and Immigration Policy Means for Major Investments

In conclusion, the Trump Administration's tariff and immigration policies will negatively impact most, but not all, investments. Excessive immigration enforcement is projected to slow the economy, while high tariffs threaten an inflationary environment – the recipe for stagflation. The table below assesses the impact of these policies on different asset classes.

Table 6

Potential Tariff and Immigration Policy Impacts

Asset Class	Likely 12-Month Impact*	Why
U.S. stocks	Negative	Higher costs (tariffs and wages) cut profits; policy swings add uncertainty, likely stagflation result
"Old-economy" metal stocks	Positive	Tariffs protect U.S. steel & copper makers.
Bonds (2-year)	Neutral	Fed may wait longer to cut rates if inflation stays high.
Bonds (10- and 30-year)	Negative	Investors demand higher interest to offset inflation and bigger federal deficits.
Real estate	Moderately Negative	Higher mortgage rates hurt buyers, fewer immigrant workers slows home-building, increases labor cost
Cash / money-market funds	Neutral	Comparatively high yields with low risk

*Assumes tariffs start August 1 and immigration enforcement tightens.

Table 7

Key "Trigger" Dates to Watch

Date / event	Market-Friendly	Market-Unfriendly
July 18-22 – Judge rules on tariff freeze	Tariffs paused: inflation risk down, stocks up, long yields down	Tariffs start: prices go up, long yields increase
Late September – Congress funds (or not) large-scale deportations	No extra funding: wage pressure eases	Funding approved: labor shortage risk increases

Trump's Pressure Campaign to Influence the Fed and Interest Rate Policy

The Federal Reserve Bank (Fed) is the national bank for banks. It sets the overnight interest rate (Federal Funds rate) that banks charge for borrowing and lending to each other. By adjusting this interest rate, the Fed can encourage (with low rates) or discourage (with high rates) lending in the broader economy. While the Fed doesn't always get the economic forecast right and must course correct at times, it is highly respected throughout the world for its political independence.

President Trump wants lower interest rates to stimulate the economy and boost the value of real estate and financial assets. He has made no secret of his desire to get rid of Jerome Powell, the current Fed Chairman and a Republican whom he appointed in his first term (and Biden subsequently re-appointed). Powell and members of the Federal Open Market Committee (FOMC), who vote on interest rate policy, are resisting lowering rates because they are concerned that lower rates, when combined with administration actions on tariffs and immigration, would stimulate the economy too much and increase inflation. The Fed believes the economy is in good shape with low unemployment, and it doesn't need the help of lower rates.

The Trump administration's tariff and immigration policies have created uncertainty regarding the path of inflation and indicate the *likely* path of inflation is *higher*.

While Powell and the Fed made a big mistake characterizing post-pandemic inflation as 'transitory' (which I didn't buy and said as much in my newsletters), I believe that current Fed policy is the prudent approach (e.g. *before lowering rates we need to wait and see how the administration's trade war and immigration policy plays out*). Expect markets to react negatively if it looks like Trump is gaining the upper hand in influencing Fed policy.

What's Next for the Economy

At times it appears like Trump is using the Hollywood Western technique of fanning the revolver while shooting from the hip. His supporters see him as a man of action, keeping his promises while his detractors see it as dangerous with bullets flying everywhere (which is what happens if you actually fan a revolver). Both descriptions are accurate.

Here are some likely outcomes:

1. **Higher tariffs = higher import prices = higher consumer prices** How much higher is yet to be determined.
2. **Strict immigration limits = fewer workers = higher consumer prices** Fewer workers raises wages and service prices in some sectors, adding to inflation from a different angle.
3. **Investments**
   - Regular U.S. stocks and long-term bonds look fragile if both policies bite.
   - Cash / Equivalents stable, susceptible to Fed changes in short term rates
   - Some U.S. metal producers could be winners.
4. If tariffs **and** large deportations both proceed, economists warn of a "stagflation" mix—slower growth **plus** stickier inflation—a tough combo for most investments.

These policy milestones will influence prices and markets. On the plus side for stocks, the recently passed One Big Beautiful Bill Act is essentially a spend and not tax / not regulate bill. It is a plus for stocks and the economy in the short run and a negative for bonds and real estate as more government borrowing implies higher interest rates.

At the same time, the AI momentum in the tech sector is undeniably impressive, despite its vulnerability to an adverse geo-political event (i.e. Chinese blockade or invasion of Taiwan and subsequent cut off Taiwan Semiconductor whose chips are critical to AI development).

Yesterday (July 16), Trump surprised markets and many China hawks by announcing a deal that lifts restrictions on NVIDIA and others selling advanced AI chips to China. In my last newsletter, I said that Trump had underestimated China in his trade negotiations. China had hit back with restrictions and outright bans on rare earth elements that are critical to making products for the tech, defense, energy and automotive sectors. The deal *potentially reduces* the incentive for a Chinese blockade and / or invasion which is a *very intentional focus* of Chinese military planning.

Bottom Line

I believe that the markets are bristling with a combination of risks that investors are not being adequately compensated for. Markets are dealing with a unique and complex blend of macro-economic factors yet treating them as business as usual. Despite the evidence, the market seems to overly discount Trump's tariff actions (e.g. TACO trade: Trump Always Chickens Out). My take is that Trump is *very effective* at getting what he wants.

Our client portfolios are invested safely and have not been affected by all the above. Some may find this a relief, while others may see the situation as a potentially missed opportunity.

If you see current stock market developments as a potentially missed opportunity, please call me! We can quickly establish an investment in your area of interest. Recently I bought exposure to European stocks for a client based in the UK / Germany who felt that the weak dollar, and long period of European stock under-performance vs the US stock market, made those stocks a relative bargain.

I'm working on a special report in which I'll examine another unique risk factor: **the potential for enormous wealth concentration stemming from unprecedented white collar job losses due to AI**. AI induced layoffs have begun and there is a serious debate about whether AI will follow previous periods of technological advancements which overall create more new jobs, industries and prosperity than is eliminated or be a deeply negative 'Great Depression' like employment shock.

Please feel free to contact me if you have questions, comments or requests:

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Your feedback is important!

Endnotes

1 https://en.wikipedia.org/wiki/Smoot%E2%80%93Hawley_Tariff_Act

2 AI calculated the implied odds based on the weighted averages of:

- Congressional vote math
- Historical court behavior
- Published macro scenarios (Moody's, Brookings, Dallas Fed), and
- Real-money betting odds