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Investment Insights into Current Events

DiMeo Schneider & Associates, L.L.C.

TARIFFS, TRADE WARS & MARKET VOLATILITY

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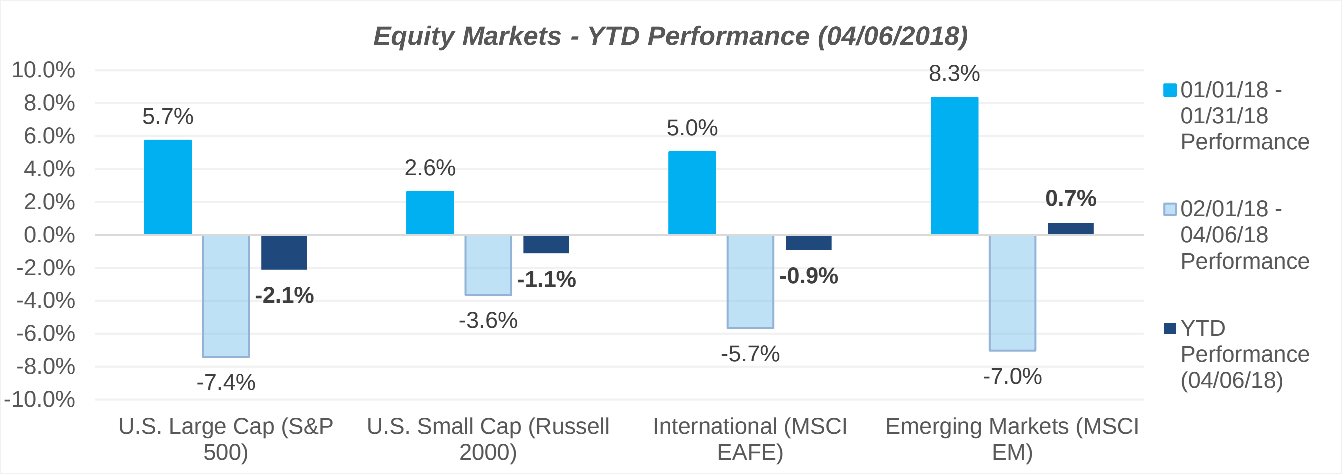
Whereas markets produced strong and steady returns throughout 2017, market returns have been far more mixed and volatile in 2018. A variety of factors contributed to this year's volatility, the most recent culprit being rising tensions over trade between the U.S. and China. A series of recently announced tariffs has increased concerns for a broader potential trade war, in turn, weighing on markets.

Volatility Returns

	S&P 500 Index (01/01/2017 – 04/06/2018)			
Year	Total # of Trading Days	# of Trading Days with Moves Greater than +1% or -1%	# of Trading Days with Moves Greater than +2% or -2%	Largest Intra-Year Peak-to-Trough Drawdown
2017	251	8	0	-2.8%
YTD-2018	66	27	8	-10.2%

Note: Peak-to-trough drawdown calculations are based on closing day values (not intraday values).
Source: Yahoo Finance 'Historical Data' tool

President Trump's announcement late last week indicating a consideration of tariffs for an additional $100 billion of Chinese goods dragged down equity markets by 1% to 2% last Friday, leaving equities with flat to slightly negative performance for the year.



Source: Morningstar Direct

Why Tariffs?
A tariff is a tax most commonly applied to imported goods. In the U.S., the tariff (tax) is collected by a customs broker or agent when goods enter the country. The goal of a tariff is to make U.S. goods more attractive by increasing the price of foreign goods.

While a tariff might benefit a domestic producer, the tariff raises the cost for businesses that use the impacted good as part of the production process. Businesses affected by the tariff generally have a few options: cut costs elsewhere, absorb the cost of the tariff (or accept lower profit margins) or pass the increased cost along to the consumer.

The Trump Administration stated that the tariffs are aimed at creating a fairer trade environment. Treasury Secretary Steven Mnuchin said in a recent CNBC interview that the United States' objective is not to engage in a trade war with China, but to instead put American interests first. In a separate interview, Secretary Mnuchin noted, "Whatever happens in trade, I don't expect it to have a meaningful impact on our economy."[1]

What Tariffs?
In recent weeks, the U.S. and China have made a series of 'back-and-forth' tariff announcements. The current tariff proposals would cover approximately $50 billion worth of U.S. and Chinese goods, though President Trump announced on April 5th that he was considering additional tariffs covering another $100 billion worth of Chinese goods. The Peterson Institute for International Economics provided the following analysis of the current tariff proposals:

Value of 2017 U.S. exports to China affected by Chinese tariffs	$49.8B	Value of 2017 Chinese exports to the U.S. affected by U.S. tariffs	$46.2B
Larger aircraft	$16.3B	Televisions	$3.9B
Soybeans	$12.4B	Midsize cars	$1.5B
Larger passenger vehicles	$6.5B	Aluminum alloy	$1.1B
Propane	$1.7B		
Electric Vehicles	$1.5B		
Cotton	$1.0B		

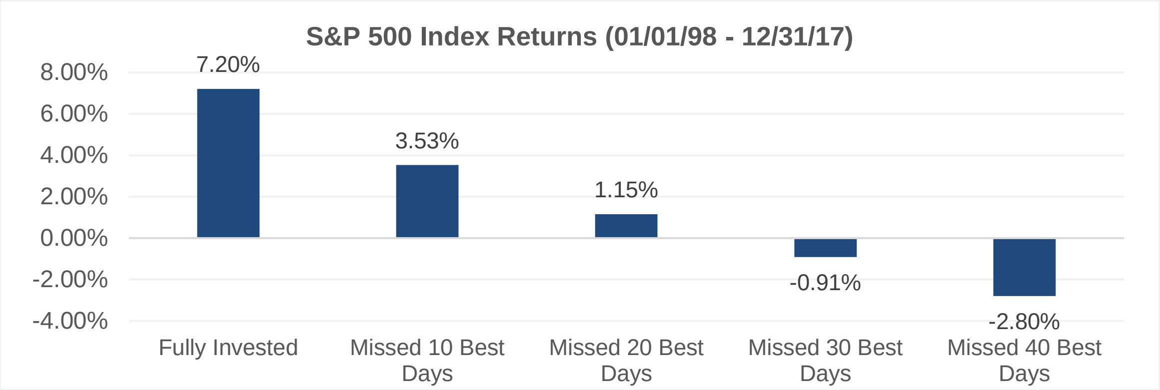
Source: Sender, Hannah, et al. "All the Goods Targeted in the Trade Spat." The Wall Street Journal, 5 April 2018.

Trade War Ahead?
It is uncertain whether the recent salvos between the U.S. and China will ultimately produce a trade war. And it could still be quite a while before the announced tariffs go into effect (if at all). U.S. companies have until May 22nd to object to proposed tariffs. After May 22nd, the U.S. government has 180 days to decide whether to proceed with the proposed tariffs. In a recent press briefing, White House press secretary Sarah Huckabee Sanders commented, "It'll be a couple months before tariffs on either side would go into effect."[2] Given this timeline, there is still time for a more amicable solution other than retaliatory tariffs to emerge.

What to Expect & How to Respond

Investors are understandably concerned about potential ramifications of a trade war with China (and possibly other trading partners), though it is simply too early to conclude to what extent tariffs will be utilized and what the ultimate impact will be. Amid the current uncertainty, investors should consider the following:

1) **Beware the dangers of extrapolation**
   While it is fair to conclude that a trade war would be a drag on economic growth, it is impossible to know what trade policy might look like several months from now and how markets might respond thereafter. As the adage goes, investors should focus on "time *in* the market, not *timing* the market." The chart below illustrates that missing just a few good days in the market can have a significant impact on long-term returns. As counterintuitive as it may seem, some of the market's best days occur during periods of heightened uncertainty; over the past 20 years, 6 of the S&P 500's best 10 days occurred within 2 weeks of the index's 10 worst days.



Source: JPMorgan Asset Management "Guide to Retirement (2018 Edition)"

2) **Expect volatility to continue**
   Investors should consider the low volatility environment of 2017 an anomaly, rather than the norm. Continued uncertainty surrounding U.S. trading relationships, the Brexit negotiation, North Korea, etc., are just a few of the items that could continue to drive market volatility.

3) **Revisit your target allocation**
   Given the extended bull market for equities over the past several years, some investors may have overestimated their willingness to withstand market volatility. The most recent market pullback is a good reminder of the risks inherent with investing. Investors are encouraged to revisit their long-term goals and evaluate risks being taken to achieve those goals. During periods of heightened volatility, investors often feel the need to "do something", though short-term, reactive moves are often ill-timed and can significantly impair the effectiveness of a well-designed investment plan. So long as circumstances and long-term objectives have not changed, investors should adhere to their long-term investment plan and should thoughtfully rebalance over time.

For more information, please contact any of the professionals at DiMeo Schneider & Associates, L.L.C.

[1]"Transcript: Treasury Secretary Steven Mnuchin on 'Face the Nation," April 8, 2018." *CBS News*, 8 Apr. 2018, www.cbsnews.com/news/transcript-treasury-secretary-steven-mnuchin-on-face-the-nation-april-8-2018/.
[2]Zumbrun, Josh. "Tariff Showdown Shifts to Intense Negotiation Period." *The Wall Street Journal*, 5 Apr. 2018.

About the Author:

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Nick provides investment consulting services to nonprofit organizations, corporate executives, family trusts and other high net worth investors. He services clients by providing advice and expertise on asset allocation, portfolio design, investment policy statements, manager search process and overall investment management. Nick is also a member of the firm's Core Investment Strategy Group. Prior to joining the firm in 2007, Nick was a Senior Financial Planner with The Ayco Company where he provided comprehensive advice to affluent clientele. Nick earned a BA in Finance and Economics from the University of Illinois at Urbana-Champaign. He obtained the designation of Certified Financial Planner (CFP®) from the College of Financial Planning and is a CFA® charterholder and member of the CFA Society of Chicago. Nick enjoys long distance running (having completed three marathons and multiple half-marathons) and spending time with his family.