Great Investors Don’t Get “Tariff-ied” Transcript

[00:00:00] Hey everybody. So unless you’ve been living under a rock, you are aware that the administration this week published its official plans for tariffs for international trade, and the stock market has promptly been in free fall over Thursday and Friday, just two trading days. The s and p 500 was down by just about 10% in the aggregate of two days, 5% each of the two days.

So, to say the least, and please forgive the pun, the stock market and many people that you talk to are currently “tariff-ied.” Everybody’s really worried, so I thought it’d be worth coming on here to share some observations about tariffs in general.

What I think the administration is trying to accomplish and what I think might be the outcome of that. And then, probably more importantly, to just talk about our investing philosophy and how I think that you could be able to navigate this time in this volatile [00:01:00] time with outstanding success.

And that’s really what we hope to try to do, is to help our clients and friends to become outstandingly successful investors. And I think this is an opportunity to do that. So, taking a step back, maybe first let’s talk about how tariffs work and what they are. I know there’s been a lot of press out there about tariffs.

So probably everybody by now knows what I’m about to say, but, so a tariff is a tax, of course, that is paid on, international trade. It’s paid on imports. It’s not a tax that’s paid by the foreign exporter sending goods into the domestic country, but it’s paid by the importer, who brings those goods into the country.

Typically, then that importer is gonna pass along that tax to the consumer in the form of a higher price. So, for example, if you buy A BMW for $50,000 and then all of a sudden your home country puts a 10% tariff on BMWs. Now the importer has to pay a tax of $5,000, [00:02:00] which they’re likely to pass along to you in the form of a higher price for the car.

And so now the, the price sticker price of the Beamer is gonna be marked up to $55,00. And so, on the surface, this is obviously inflationary prices go up and that is if we think about the key criticism of the tariff police. That’s probably the, the most important one. And that is that this is inflationary and we just, you know, went through a couple of years of trying to fight inflation and now all of a sudden this could be another catalyst for inflation to re-spark here in the United States.

And that's a big concern and especially even worse if you turn this into a trade war where we raise tariffs on other countries, they turn around and raise their tariffs on us. We reciprocate, they reciprocate, and you have this upward spiral of trade war, you know, that's problematic.

Then that makes not just prices go up and inflation happen, but it also just [00:03:00] makes international trade slow down and, and get bogged down because there's a lot of uncertainty and nobody wants to trade with one another 'cause we're just hammering each other with taxes.

You know, one of the purported benefits of all this is that it would bring manufacturing back to the United States. Yeah, that may be true, but in order to tool up and to build manufacturing facilities and to kind of build the capacity for us to manufacture all this stuff would cost us a lot of money and a lot of time, thereby also causing prices to go up and causing inflation to happen. That's, you know, relevant concern.

So, the bottom line is most analysts fear that this could cause a spiral of inflation, and also cause international trade to kind of decline, as well which could cause just overall economic activity to go down could cause interest rates to rise as inflation is happening. And then you'd be treated to probably the worst economic condition you [00:04:00] could have, which is known as stagflation where.

Inflation causes economic activity to decline because nobody can buy anything 'cause prices are too high and now you have a recession at the same time as you're having inflation that's known as stagflation. We haven't really dealt with that problem in the United States in the 1970s and it's a really nasty problem.

It's probably the worst economic condition you can have. So certainly not something we want to have. Whether the logic might be right or wrong, what is the actual logic? There are a couple of pieces of logic I just mentioned a minute ago. The hope is we bring manufacturing jobs back to the United States.

It's also true that the president has talked about, you know, the tax revenues themselves as being beneficial. So the White House has estimated that we could collect as much as $700 billion in, in tariff taxes. Now some have disputed that number, but whatever the hundreds of billions of dollars number might be that you could help to offset income tax, you [00:05:00] could deliver income tax cuts as a result of collecting tariffs, which could be a good thing because in general, that substitutes a consumption tax for an income tax, at least at the margin. And in so doing, there could be some economic benefit from that as well. Really, in my opinion, the, the primary benefit that the administration is going for is to create trade reciprocity, right?

So to, to have to level the playing field with other countries with respect to trade policy and particularly with respect to tariff policy. The way to think about it is, , that we have a significant trade deficit in the United States, and that's something that economists have been worried about for decades actually.

And I think understanding a little bit of history here is probably really useful. So after World War II, you know, the United States emerged from World War II as by far the dominant world power. We, you know, obviously we weren't directly in the line of fire of any of [00:06:00] the war theaters, for a lot of reasons.

We, we just emerged as the most unscathed and economical . We were the powerhouse of the world And one of the ways in which we were the powerhouse is we were the world's dominant exported. Every year we ran very large, , trade surpluses meaning we, we exported a lot more stuff to other countries than we imported.

And I think 1947 or so was the peak of that. Just for some context, we were at that time running a trade surplus, which is about almost 5% of our GDP came from our trade surplus and in today's numbers, that would be something like $150 billion. So we were, one of the strengths of our economy at that time was we were a very dominant exporter of goods and services.

Fast forward to today. That has totally flip flopped. Today we run a very large trade deficit . For context, our trade deficit on manufactured goods, last year was actually [00:07:00] almost 5% of GDP as well. The deficit was, and that adds up today to $1.2 trillion. So, it's a problem, you know, the fact that we have this trade deficit, and I think it's important to understand why that's happened.

That is because, you know, after World War II, we decided that we would participate in, a plan to help to rebuild the economies of the rest of the world And what we basically did was we subsidized the rest of the world and their export economies by giving them unequally favorable tariff deals, trade deals, , and in particular with, with respect to their tariffs.

So, , what, what's happened over the many years, we found ourselves in this spot where, other countries tariff our stuff a lot more than we tariff their stuff coming back into our country. And that, that's been identified as the real problem we're trying to get to here is that we're just being treated unfairly with respect to international trade.

Just for some context around [00:08:00] tha . So. , and continuing the, actually the example of BMW, so Peter Navarro, who is one of the senior White House advisors on this particular policy, , was on TV recently, and he, he singled out Germany in with respect to auto tariffs particularly, and he called the auto tariffs in, in the EU, grossly unfair because the EU puts a tariff of 10%.

On American cars coming into the EU, while we put a tariff of 2.5% on European cars coming into America, and in addition to which in Germany, they also have a a 19% value added tax. So in his view, A BMW coming into the United States is taxed much less than a Cadillac. Going into Germany is a result of that.

BMWs are just artificially, a lot cheaper than Cadillac's are to export and, and that's not fair. So I do find it a little interesting to hear a lot of our trading partners, . You know, [00:09:00] screaming and complaining about administration trying to fix this problem because in essence, we've been subsidizing their economies for 75 years now.

You know, we have benefited from that because in many ways what we've done is we've shipped a lot of our low margin. Lower income, lower wage manufacturing functions offshore to places that are willing to do those functions for cheaper. While we've kept the information economy and the sales and marketing economy here in the United States and, and that is true, and so we've been a beneficiary of offshoring manufacturing as well.

But, but by and large it is true that one of the ways we've kind of. Become, a less wealthy and less productive economy is because we have subsidized global trade for, for other . And, you know, many economists differ on how big of a problem that i . But where I come down on this personally is, you know, Warren Buffett back in 2003 was interviewed and he [00:10:00] said, and, and this is what I agree with, he said that these trade deficits sell our country short and.

It's basically effectively transferring our wealth to other countries. And he likened it to selling off pieces of our country. And that's how I feel about i . Mean I, I really believe, you know, at this moment in time, 75 years later, you know, we were at one time the richest nation on earth. But if you look at our government finances now, we are pretty seriously in the red and we can't afford to subsidize trade for other countries anymore, in my particular opinion.

, and I would say it seems like the stock market agrees with that sentiment. , I think one thing that wasn't really publicized very widely but is true is that on Wednesday when the president was making his famous rose garden speech about tariffs, and he opened the speech talking about how his goal was to get reciprocity of tariffs equal footing with other countries.

So if you tariff us [00:11:00] 5%, we're gonna tariff you 5. And when he was talking that way and talking about reciprocity. , the stock market was actually reacting really favorable. The stock market was up around 1% during that point in his speech, and then suddenly he pulled out this big chart that showed the actual tariff rates that he was proposing to apply to some of our trade partners.

And those tariff rates were asymmetrical? They were, they were, he was proposing that we would charge. Other countries, much higher tariffs than what they've charged us. And the stock market went into a free fall, went into a complete, complete tizz. So it, it was almost like he was proposing that we become punitive with other countries and the market just went haywire over that.

So, this is what it is. And you know, the, I'm sure that a lot of people, , appreciate and others don't appreciate, Donald Trump's [00:12:00] style, and the way he negotiate . But my particular take is, you know, he's been called reckles . He's been called irresponsible, for the way that he proposed those tariffs.

But I will say, we've known for decades how Donald Trump negotiate. I mean, in 1987, he wrote a book called The Art of the Deal, where he talked about what you do in a negotiation is the first round you ask for the moon and the stars hoping that as you go through the negotiation, you end up in a much lower place where you hope to be in the first place.

So that's the way he negotiates, love it or hate it. That is the way that he looks at negotiating. And in my particular opinion, you know, of course I could be proven wrong about that, but this is what he's hoping to do, is he's proposing these, you know, very punitive, asymmetrical, tariff proposals on other countries.

But knowing that that leaves him room for [00:13:00] negotiation, and it kind of almost like gives them shock and a so that eventually they will come around to a place where we can have tariff equity at tariff reciprocity, and hopefully at a place where everybody's tariffs are lower than they are today. I mean, that, that would be ideal, of course, is that we all agreed that we're gonna tariff each other the same, and those tariffs are gonna be at, at a low or zero rate.

Love it or hate i . My personal opinion is that is exactly what happened and then you gotta, you know, wonder about whether that's gonna work you know, obviously he, he's playing a very high stakes game of chicken. There's no guarantee that that, that he's gonna win that game and of course the downside is that is not pleasant, right?

If, if, if, if, you know, other countries do decide that it's time to retaliate, then now we do have a problem, right? Like, you know, this trade war I was talking about before, . [00:14:00] But you know, my personal opinion on this, and of course nobody knows how this is gonna work out, but I do believe that we, America has an advantage in these negotiations and a very strong hand because of the fact, like I said before, we do have very large trade deficit, meaning we import a lot more stuff from our trade partners than they import from us.

And so, you know, if we become more punitive on tariffs, it, it cuts them harder than it does u . So I do believe we have the negotiating power in these discussion . Now that doesn't mean that we're gonna win out or that, you know, we're, this is gonna be a good outcome but I do believe we, we at least have that advantage.

I think it was interesting when you look at the tale of two countries, if you will, on Friday, I. So in response to these proposals, China, on the one hand came out and was very [00:15:00] hawkish with us and said that they're gonna reciprocate by applying 34% tariffs against everything that we export into China.

When I thought about that, you know, the fact of the matter is. , we import four times as much stuff from China that they import from us, so they've got more to lose if international trade between the two of us goes south. Not to mention. The stuff that they import from us is very largely food and energy.

They already are having trouble feeding their people, so the idea that they're going to continue to really make food imports a much more expensive to their own people I don't know. I just take with a little bit of a grain of salt, we will see . But that is the fact. Now, on the other hand, the other country that I would think about or point out is Vietnam.

So Vietnam, I think it's really interesting, and not a lot of people talked about this, but [00:16:00] on Friday the stock market was down 5. The s and p 500 was down 5. But Nike stock was up 3. It's really odd. I mean, it's literally an 8% delta from the market. And why did that happen? Well, it was because Nike makes most of their stuff in Vietnam, and the Vietnamese basically signaled to the White House that we're willing to come to the table and negotiate.

So if more countries followed that example and followed Vietnam to the negotiating table. You could find that there's a little bit of a scramble that everybody's trying to, you know, get to the White House to get to, to the negotiating table with the White House so that they can cut a good deal before everybody else does.

Of course, time will tell. So more importantly, let's talk about the impact of all this on, on you as an investor and what I believe, you know, what our investing philosophy would say about all this. So one of the, my favorite quotes that we use all the time, there was a famous movie producer called William Goldman, and one time Goldman was [00:17:00] asked, how do you know what's gonna work in the movies?

How do you know, you know, whether a picture that's coming out is gonna be successful or no? And he said nobody knows nothing, right? Nobody knows. , and so everything I just said is my opinion, but of course, I don't know. And anybody who says they do know how this whole tariff tussle is gonna work out is really lying.

And actually you shouldn't listen to 'em in the first place. There are a million different moving parts to this. Our very firm belief is that making investment decisions based on the emotions of daily geopolitical or economic or financial events of the day is the biggest mistake an investor can make.

We believe that an investment philosophy is superior to an investment outlook because really at the end of the day, I. Anybody's outlook is really nothing but a guess. Nobody really does know. So the way a successful investor handles this, in my opinion, a great investor can be outstandingly [00:18:00] successful during a time.

Like right now, is that, you know, just listen to the words of J.P. Morgan who once said that Bear markets are a time when stocks are returned to their rightful owners, and that basically means, you know, the s and p 500 has returned 10% a year over time, so, so stock owners or equity owners have been rewarded and endowed with 10% per year in returns.

But you don't just get those return. You don't just, they don't just fall outta the sky. You have to deserve them, and the way you deserve them is by keeping a cool head. During times, like right now, during times when you're really scared, staying calm. So one of the key premises to our investing philosophy is that in order to be a real equity investor in order to deserve it, you can't think about big high flute and concepts like the market or the economy.

You can't think of the stock market as this big casino and stock prices as [00:19:00] poker chip. Stocks are shares of certificates in of ownership in individual businesses, in great businesses, businesses that you probably patronize on an everyday basics. If you own shares of Amazon, you own a part of the business that you patronize probably every single week.

And so to be a great investor, you have to have unfailing faith in the fact that the capitalist and entrepreneurial managers, these businesses that you own, no matter what geopolitical or tax or economic problem that you put in front of them, they're gonna innovate their way around in. They're gonna figure it out, and they're gonna excel and they're gonna prosper on your behalf.

They always have done that every single time historically, and if you don't believe that, they'll do that again. Then you probably shouldn't be an equity investor in the first place. So, legendary investor, Benjamin Graham, he actually used to talk about this [00:20:00] allegory, which was, he called it Mr. Market and all the irrational and contradictory emotions of the market.

He, he pulled, pulled them all together in the form of what he called Mr. Market and his observation was that Mr. Market was always tempting you to make the big mistake. And right now, that's what's happening right now. Is the serpent whispering in your ear ? Okay, it is. Hey, you're smart. You can see this is gonna be a mess.

You can see that the recession's coming Why don't you just hop outta stocks for a little bit and then you can just hop back in as soon as things settle down. Well, this is the big mistake. The odds if you do that, the odds are overwhelming, that you will someday either regret buying back your portfolio at a higher price than you sold it for, or even worse, never buy it back and you'll miss out on that 10% return for the rest of your life.

Because if you sell your stocks [00:21:00] today, one of two things is gonna happen either. This week, Wednesday, some country says that they're gonna come to the table and create a, a trade deal with the United States, and stocks are going to skyrocket. And you're gonna find yourself in this situation where you are wrong and you have to buy back your portfolio at a higher price, or worse, it goes the other way.

This is even worse. You were right. Stocks go down more this week and you sit back feeling really happy with yourself, and you say to yourself, I'm gonna get back in the market as soon as things settle dowe. Well, I'm here to tell you that when things settle down, it will have meant the stock market went much higher and is now higher than what the point you sold for, and you're found buying your portfolio back at a higher price.

I've seen this happen. I've done this, I've seen clients do it. I promise you that is what will happen in my career. I, I always say, , people talk about the fact that the, the dominant emotions in [00:22:00] stock market investing are fear and greed. Actually, I believe the dominant, emotion in stock market investing is regret.

And in my career, there are three moments of keen regret that I can bring to mind that are carved in my memory forever. The first was at the end of 1999. The s and p 500 was at 145. Right before the tech market bubble happened, the tech market bubble brought the market down by 50. Okay?

People who sold in the teeth of that, it brought it down to eight 8. People who sold in the teeth of that market missed the ride from eight 8. To 5,100 today, and then the fall of 2007, the s and p 500 at that time was 150. Next thing you know, it loses more than half to a level of about seven 5. Okay?

People who sold into the teeth of that one when things were so terrible, missed the ride from seven 50 to 5,10 . And then in Covid, you [00:23:00] remember that one, well, February of 2020, the s and p 500 was at 300. In one month, it went down 5% to a level of about 2,50. Well, people who sold into the teeth of the covid decline missed a double to 5,100 today.

Okay, so don't, don't regret, okay. Have faith, just like the tech bubble burst, just like the great financial crisis and just like Covid The only thing I can say about those three times, my main regret is that while they were happening, I didn't buy more. Let me say that one more time so you really get what I'm saying.

The regret I have about the great bear markets I've lived through is that while they were happening, I didn't step up and buy more. Maybe that can give you an idea of what you should be doing this week. This too shall pass, and when it does, I can promise you stock prices will be making new all time highs.

You can count on that. So I hope this was valuable. I hope you liked it. [00:24:00] Please, I love your comment . I love to hear about what you thought about thi . Please feel free to send me a question or a comment or like this on social media, even if you didn't like it. Love to hear from you, so thanks for listening and enjoy the spring weather.

Talk to you soon . Bye.