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I'm Zach Teich, retired foreign service officer and amateur investor. I was a State Department economic officer for 27 years practicing good old fashioned political economy (analyzing economic events and their impact on society, policy making, and relations with the county to which I was assigned). I'm not qualified to be a market analyst, and if I do happen to tell you what I'm doing as an investor, my best advice is…do the opposite! Therefore, I bring a different perspective than most to the Forum - I tend to look at factors external to the markets that help form the investment climate and only then examine stocks themselves.

I'm pinch-hitting today for a very qualified market analyst, David Toms, who is ill. So my presentation will contain no slides or charts, and I'll give you only the bare minimum number of statistics needed to create a context for my remarks.

We meet at the start of a new calendar year and a new Presidential administration. Anyone who tells you he/she knows where the economy and the markets are going is lying. Many things in the policy environment are changing, and those changes will impact the investment climate. All any of us can do it make reasonable guesses at this point in time.

To know where things may go, however, it helps to know where we are now. Looked at from the domestic macroeconomic perspective, the economy is in very good shape. While end-or-year numbers on GDP growth are not yet out, it appears likely that we experienced real GDP growth of 3% last year. The inflation rate as measured by the CPI was 2.9% for CY '24, down significantly from 4.1% in 2023. The unemployment rate was 4.1%, which was fractionally higher than 2023's 3.8%. The Fed reduced interest rates three times last year, dropping the federal funds rate by a full percentage point over that time. Essentially, the numbers indicate that we achieved a soft-landing - we brought inflation down from the 2022-23 inflation spike without a recession. However, interest rates faced by consumers - particularly home mortgage rates - remained stubbornly high, and the Fed didn't achieve its 2%/yr inflation target. The national debt reached approximately $34 trillion, an amount equal to our nominal GDP. Annual debt service approached $1 trillion. There is a healthy debate underway regarding the sustainability of the debt and debt service numbers. We ran overall balance of payments deficits (goods and services basis) of approximately 3% of GDP in both 2023 and '24.

Where did the market move in 2024? Up. Way up. The S&P 500 had its second consecutive year of over 20% growth, which is the first time since 1998/99. The question for us, though, is: where is it going THIS year? The policy environment created by two actors - the Fed and the Trump Administration- will have a great deal to say in answering that question.

The Fed has already spoken. In its last meeting of 2024, it announced that it will moderate the pace of interest rate reductions to keep downward pressure on inflation. Thus, consumers can expect to continue earning a decent and positive rate of return on savings, but borrowing costs will continue to be higher than hoped, and stimulus via rate cuts will be lower and less frequent than the market had earlier anticipated. Accordingly, GDP growth could be constrained, and the market's potential upside could be lower.

The Trump administration is only two days old, but to my mind its decisions (and those of the GOP-led Congress) will play a huge role in framing the investment climate. Here's an example. On March 14, two separate but linked alarm clocks will go off on Capitol Hill: the

current CR will expire; and the Fed will run out of “extraordinary measures” it uses to keep making payments without breaching the legally established debt ceiling. Markets are very sensitive to these two issues, and as of now, we don’t know how they will be resolved. The government could shut down. We could default on the debt. I think either is unlikely - but both are possible. We can expect market volatility to increase the closer we get to the deadline.

Here’s another example of how economic policy will impact the investment climate. President Trump has promised to “drill baby, drill” to achieve “energy dominance.” All other things being equal, more oil/natural gas supply should increase our petroleum and LNG exports. (We are already the world’s largest oil producer and LNG exporter, and a great deal of our 12 million barrel per day oil production is exported as many domestic refineries are optimized for imported heavy crude.) This will improve our balances of trade and payments. Moreover, increased production would exert downward pressure on global oil prices, and help lower inflation. Markets should love all of that, and “oil patch” stocks might soar.

Other economic policy issues also will have a direct bearing on the investment climate. The President has said that he intends to place higher tariffs on imports from Mexico, Canada, China, and perhaps even the rest of the world. Since importers pay the tariffs to the government, and typically pass along the cost to consumers, price increases on imported goods can be expected. Will that spike inflation and cause either a further delay in Fed interest rate cuts - or even rate increases? If so, markets can be expected to react negatively. There is another Presidential policy that we need to factor-in when examining the investment climate - the promise to aggressively enforce immigration laws. Mass deportations may be very expensive, reduce the labor supply, and push up costs in both the agriculture and service sectors. These impacts all would fuel inflation, reduce consumer confidence, and weigh on stocks.

Outside the policy realm, how things get done - or not - in Washington also will influence the investment climate. The President has said that he wants “one big beautiful bill” under Senate reconciliation rules to cover the following: extending and broadening the tax cuts that expire at the end of the year; immigration; and raising the debt ceiling. Given the narrow GOP majority in the House, and the impending deadline on the debt ceiling issue, is this likely to happen? How will markets react if it doesn’t? All other things being equal, markets should welcome a clean extension of existing tax policy, but how would they react to additional tax breaks that would increase the deficit? Conversely, how would they react if the GOP fails to get the tax bill passed at all, and taxes revert to their earlier (and higher) rates?

Finally, what is likely to happen about cutting government spending? Federal spending accounts for approximately 20% of GDP. 2/3 of that spending is mandatory (debt service, Social Security, Medicare/Medicaid). 1/3 is discretionary, (the largest item being defense), and is funded by annual appropriations. So in round numbers, about 7% of GDP is in play for the budget cutting. DOGE is supposed to make recommendations to the President and Congress about what to cut. Here is the dilemma. If you don’t cut significantly, deficits increase, particularly if more taxes are cut as the President desires. Cut too deeply, though, and GDP growth may be adversely impacted because of the spending cuts themselves, and the reduced economic activity and rising unemployment they bring. Markets may not welcome either outcome.

In conclusion, my crystal ball is murky. In past years, I could have given you a simple statement to guide your development of investment strategy like “don’t fight the fed” or “there is no alternative” to investing in stocks. I can’t do that this year because the policy environment in

which we invest simply is too opaque right now. Those of us who are market optimists have good reason for for their views given the strength that the markets themselves have shown over the past two years. Market pessimists would caution that there is equally good reason to be wary because of the potential policy headwinds they see. So all I can say is this: put your money on either red or black and spin the wheel!