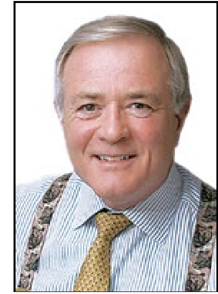
DJC
THE DAILY JOURNAL OF COMMERCE, PORTLAND, OREGON


William Rutherford

Markets dance to a new tune, with politics on center stage

Published Feb 10, 2025

An old market adage is: “As January goes, so goes the year.” If that holds true, 2025 could prove interesting indeed. The S&P 500 advanced 2.7 percent for the month, and the Dow Jones posted an even more impressive 4.7 percent increase. The tech-heavy Nasdaq managed to climb 1.6 percent, although not without some drama along the way.

The Federal Reserve, as expected, kept rates steady in January. Chairman Jerome Powell, in his typically measured way, emphasized that the Fed would remain “data dependent,” while monitoring inflation and growth. The market seemed to accept this stance, at least for now. And jobs and inflation numbers reported for January did not cause the market to believe that there would be any near-term change. Economists, including those at Goldman Sachs, who had been predicting three rate cuts for 2025 as recently as December, have, for the most part, tempered those calls to possibly one cut. As we have seen before, the Fed’s patience can wear thin when inflation signals appear, which could well happen with labor shortages and the cascade of new tariff announcements.

The tech sector hit major turbulence in January when DeepSeek, a Chinese startup, announced it had built an AI model that matches those of industry leaders at a fraction of the cost. Never mind that innovation drives technology forward – traders hit the panic button. Nvidia, the U.S. AI and GPU semiconductor chip leader, with its 80 percent market share in discrete GPUs (graphics processing units) and near dominance in data center GPUs, dropped 17 percent – its worst decline since October 2023. This was the largest market capitalization decline in the history of the U.S. stock market. Wall Street traders were spooked by the possibility that more efficient AI might mean less demand for expensive processors, and thus a potential contraction in capital expenditures for large language model data centers.

But here’s where a bit of economic history comes in handy. When cars became more fuel efficient, did we end up using less gasoline? Quite the opposite. As driving became cheaper, people simply drove more, pushing total fuel consumption higher. Economists, observing trends dating back to the Industrial Revolution, call this the Jevons Paradox – make something more efficient, and people will use more of it, not less. Microsoft CEO Satya Nadella made exactly this point about AI, noting that as it becomes more efficient and accessible, its use will likely skyrocket.

He’s probably right. Microsoft, Google and Meta have announced that they are not scaling back their AI investments – but rather doubling down. The market’s knee-jerk reaction to DeepSeek looks increasingly shortsighted. Cheaper, more efficient AI won’t reduce demand for computing power any more than fuel-efficient cars reduced our appetite for gasoline. If anything, it will accelerate adoption and drive demand even higher.

Then, on the last day of January, came the president’s tariff bombshell: a 25 percent tariff on Canadian and Mexican goods and a 10 percent hit on Chinese imports. Tariffs raise concerns about inflationary pressures and supply chain disruptions. The market typically doesn’t like trade wars and their associated uncertainty. A moving target of tariffs makes it impossible for businesses to plan since they are not able to judge demand, due to higher prices, or costs, due to retaliatory tariffs. Uncertainty about making business investments usually results in lagging economic activity.

The IMF projects annual global growth at 3.3 percent for both 2025 and 2026. That isn’t stellar by historical standards, but not bad considering the headwinds from war, trade disruptions, declining demand from China, ballooning sovereign debt and more. The broader economic picture, including employment and wages, remains resilient, though consumer confidence bears watching as the higher systemic costs of curbing labor mobility (i.e., reduced immigration) and the new tariffs work through the system into higher prices for services and goods.

Through all these crosscurrents, the stock market continues to find its footing. Market sectors are rotating in and out of favor as these policies play out, making stock selection more critical than ever. For those who can look past the headlines, solid companies with strong fundamentals still offer plenty of investment potential. Markets have survived trade wars, tech bubbles, and policy shifts before. And the White House’s current occupant closely follows the stock market reaction to his policies and, thus far, has adapted accordingly.

For investors, the message remains clear: maintain a steady hand. Refrain from allowing volatility to become a distraction. Be wary of emotions overcoming a long-term strategy. Stay diversified and remain invested.

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