The Flagship: An Executive Intelligence Brief

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Briefing: Wed 5, **March 2025**

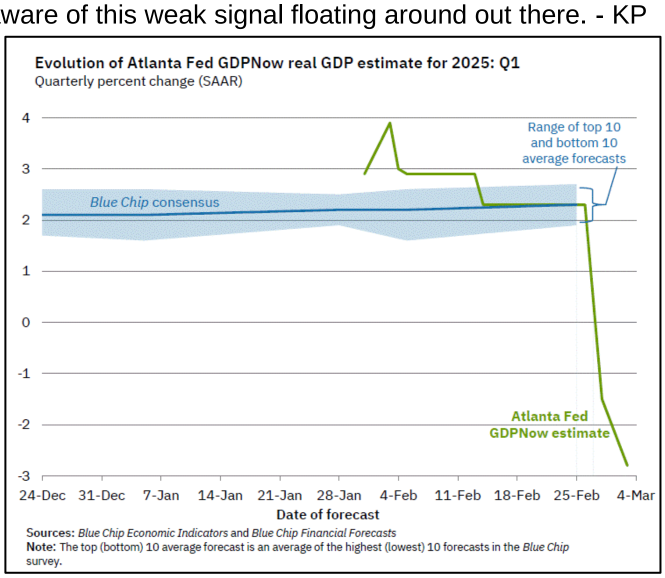
Domestic Quick Items of Interest

- **3 Rate Cuts in 2025?** I laugh at those that believe that the Trump Administration is purposefully tanking Q1 GDP to get the Fed to trim an additional interest rate cut in 2025. But whether on purpose or a by-product of what is going on, the outcome is the same. Odds are now above 60% that the Fed will give us three interest rate cuts of 25 basis points each in 2025, based on weak economic signals (see below). Whether this holds or not is another question. - KP

- **US Services PMI Hangs Tough. –** January and February can be volatile months for Purchasing Manager Surveys, and the US Services PMI is sending us a couple of signals. The first is that it remained above 51.0 points which means that it is continuing to expand. And remember that the services side of the US economy accounts for approximately 60-65% of GDP.

  But secondly, it was weaker by 1.9 points between January and February. Some of these could be weather-related disruptions after significant waves of winter weather shut down portions of the country. Wildfire also hit the west coast and was having some impacts. We don't know if this was a sign of some weakening (as we see below in the Atlanta Fed's GDPNow report), or if it was indeed just a weather-impacted reality. - KP

- **Atlanta Fed GDPNow Plummets. –** The GDPNow reading threw us a strong curve ball in its latest reading. After a sluggish Personal Consumption Expenditures reading for January, and an unexpected increase in imports (reportedly due to a significant amount of gold being imported along with firms getting ahead of tariff risk), it created a drag on GDP. The current outlook shows the forecast dropping from growth of 2.3% to contraction of 2.8%. As you will see from other reports in today's briefing, there are crosscurrents that suggest that the Atlanta Fed's data will likely adjust upward in the next revision. It would be highly irregular for economic growth to make that radical an adjustment without some form of significant Black Swan event or geopolitical event. This is a "wait and see" report but just be aware of this weak signal floating around out there. - KP



Sources: *Blue Chip Economic Indicators* and *Blue Chip Financial Forecasts*
Note: The top (bottom) 10 average forecast is an average of the highest (lowest) 10 forecasts in the *Blue Chip* survey.

Additional Items we are watching.

- **Debate Over Fentanyl. –** I heard a reporter today challenge the White House Press Secretary, commenting that the number of Fentanyl seizures at the Canada/US border was just 43 pounds, and what does the Trump Administration expect Canada to do in order to get tariffs released?

  First, I wondered if that was the case. Data shows 43 pounds of fentanyl being confiscated at the US/Canada border from October of 2023 to September of 2024. That much is true. But in the first month of January alone, an additional 10 pounds was captured after tightening inspections.

  But second, at least one provincial report cited those 46 pounds was seized in the Ontario region over two months alone, and these discrepancies are part of the problem. We don't know what the situation is.

  So, the reporter is right in one sense, it is very difficult to stop 43 pounds of anything getting smuggled into the US. But the volume is theoretically increasing and reportedly some of the manufacturing facilities making it were still operational (perhaps they have been shut down by now).

  Now, California confiscated 62,224 lbs alone and Nebraska found 119 lbs; coming from somewhere. Mexico seizures total 21,148 pounds. A lethal dose of fentanyl can be as little as 2mg. The risk is astronomical. Picking a fight over stopping fentanyl is likely worthy. - KP

Global Quick Items of Interest

- **The Exemption Game –** Tariffs are a tool and, as such, they are highly variable. The stated intent is to encourage consumers in a given nation to buy domestically made products rather than imports but the real function of a tariff is to persuade nations to shift policy in one way or the other. A tariff is threatened unless a given policy or action is pursued. This has already happened with the US tariff policy and will continue to. There is also a great deal of adjusting as the impact of a given tariff is assessed. **The Trump imposition of a 25% tariff on Canada and Mexico may well be suspended for the auto industry and there are discussions around food as well.** The real target of these tariffs remains China as there has been a surge of Chinese investment in Mexico as a way to dodge the tariffs on China itself. The tariff game is extremely fluid and will be shifting almost daily. It becomes a matter of who has the most leverage. CK

- **Foreign Aid Battle Rages On –** The decisions made by the Trump administration have gutted most of the foreign aid programs the US has been engaged in for decades. A lower court held that suspending these already allocated funds was not legal and the issue went to the Supreme Court. **It was a 5 to 4 vote but the lower court position was upheld and the $2 billion in foreign aid will be distributed as planned.** This is another setback for the Trump plan to cut foreign aid universally. Much of the aid effort over the years has had dual purposes. On the one hand it is an expression of US "soft power", a way to keep nations allied to the US but it has also been used to stimulate business development in the US. Construction projects funded by these funds generally required acquisition of Caterpillar equipment. On average over 90% of foreign aid money never left the US as it was used to purchase goods and material from US suppliers. CK

- **Fuel Prices Likely to Increase Due to Tariffs –** Over the last few years there has been one bright spot as far as inflation threats were concerned. Fuel prices stayed low as the US increased its production of oil and gas. There were predictions of $150 a barrel oil and $6 gas at the pump. Instead the per barrel price has remained in a range between $70 and $90 despite hurricanes, geopolitical conflict and other factors**. The fear now is that tariffs on Canada and Mexico will affect the movement of gas and oil across borders and this drives up the price of fuel quickly**. The refineries in the US are older and designed for the heavier crude that comes from Canada instead of the lighter crude from Texas. The system is highly integrated and imposing a 10% tariff on fuel will immediately drive per barrel prices to as high as $130 to $140. This translates into pump prices between $4 and $5 per gallon. CK

- **China Sets Growth Target of 5% -** The goal for the Chinese economy this year is set at 5.0% but there are plenty of skeptics given the headwinds of a trade war with the US and the fact that Chinese consumers have yet to show any willingness to boost spending. The government is going to rely on various forms of fiscal stimulus but thus far there has been little response from either the consumer or the business community. The collapse of the property market still limits the ability of the consumer and the investor to recover. **Exports have returned to their previous place of prominence as domestic demand has not ramped up as hoped**. The trade war with the US limits what can be expected from exports but China has some tools it can deploy to keep these exports up – namely the ability to devalue the currency to offset the tariff impact. It is far easier for China to do this kind of devaluation and it is a tactic they have used in the past. CK

Additional Global Items we are watching.

- **Taiwan Worries About the US Commitment –** No nation was more shocked by the US attitude towards Ukraine than Taiwan. Taiwanese leaders are wondering if they will face the same fate. Granted, Trump is close to Vladimir Putin and not close to Xi Jinping but there may not be willingness to protect Taiwan should China elect to attack.
- The hope is that Taiwan's position as a major supplier to the US technical community will give them some leverage. Taiwan Semiconductor manufactures over 90% of the semiconductor chips used in the world and the US. This is both an advantage and disadvantage. The US needs these chips but resents that level of dependence. This has led the company to radically rethink its investment strategy. They are already building a facility in the Phoenix area and investing $65 billion in the development. That level is now increasing to $165 billion and several other major Taiwanese companies are developing their own projects. The intent is clear enough. Taiwan seeks to cement its place as a critical security and economic partner in hopes that Trump chooses to honor the commitments that have been made in the past.
- One factor that may be in Taiwan's favor is that Trump is overtly anti-China and is not sympathetic to Xi Jinping. Taiwan is an ally in a way that Ukraine never was and never would be. Taiwan's leaders seem willing to bend to any of Trump's demands as they know they can't survive a Chinese attack without US support. CK

US Domestic Economic Items

- **January Construction Data Mixed.** The January construction spending data shows that the US construction sector was mixed in the month and was showing pockets of weakness in some areas and good stability of new activity in others.

Table 1. **Value of Construction Put in Place in the United States, Seasonally Adjusted Annual Rate**
(Millions of dollars. Details may not add to totals due to rounding.)

Type of Construction	Jan 2025ᵖ	Dec 2024ʳ	Nov 2024ʳ	Oct 2024	Sep 2024	Jan 2024	Percent change Jan 2025 from - Dec 2024	Jan 2024
Total Construction	**2,192,540**	**2,195,985**	**2,184,796**	**2,176,627**	**2,142,427**	**2,122,229**	**-0.2**	**3.3**
Residential	**944,481**	**948,762**	**936,848**	**934,237**	**903,941**	**915,398**	**-0.5**	**3.2**
New single family	431,246	428,545	423,953	422,628	419,907	435,000	0.6	-0.9
New multifamily	116,932	117,809	118,561	121,279	123,277	132,883	-0.7	-12.0
Nonresidential	**1,248,058**	**1,247,223**	**1,247,949**	**1,242,391**	**1,238,485**	**1,206,831**	**0.1**	**3.4**
Water supply	34,334	34,243	35,095	35,354	35,367	29,614	0.3	15.9
Amusement and recreation	41,363	41,327	41,886	41,873	41,506	36,446	0.1	13.5
Public safety	19,096	19,139	19,391	19,567	19,237	17,411	-0.2	9.7
Sewage and waste disposal	47,015	46,835	47,135	47,404	47,242	43,120	0.4	9.0
Transportation	70,093	70,013	69,684	69,926	70,018	65,448	0.1	7.1
Educational	134,701	135,553	136,434	135,250	133,151	126,055	-0.6	6.9
Religious	4,662	4,590	4,603	4,339	4,067	4,399	1.6	6.0
Manufacturing	235,749	236,535	236,377	236,777	236,805	223,104	-0.3	5.7
Office	104,781	104,317	103,308	103,455	100,602	100,928	0.4	3.8
Power	151,842	151,329	151,098	148,803	148,438	146,801	0.3	3.4
Communication	29,139	29,071	29,093	28,858	28,760	28,595	0.2	1.9
Lodging	23,494	23,330	23,298	23,404	23,479	23,576	0.7	-0.3
Health care	69,339	68,944	70,163	68,523	68,454	69,830	0.6	-0.7
Conservation and development	11,431	11,360	11,498	11,459	11,584	11,593	0.6	-1.4
Highway and street	146,064	145,172	143,616	143,019	144,168	149,196	0.6	-2.1
Commercial	124,956	125,467	125,270	124,379	125,608	130,717	-0.4	-4.4

First, top line construction was still trending at nearly $2.2 trillion, growth of 3.3% Y/Y despite some softness of 0.2% M/M.

Second, residential construction was sluggish. Single family construction was obviously facing some interest rate and cost of construction headwinds. Until the 10year Treasury comes down further, interest rates will stay higher and new starts and permits will be lower as we saw in January. The 10Y Treasury has been softening of late, the yield rate dropping generally at a snail's pace, but the administration recognizes the problem and is working to get it down faster.

Multi-family construction moves in some broader cycles. After going through a period of time in which some moderate overbuilding in some markets has kept new multifamily starts lower, 2025 is expected to see some mild rebound in some areas. Granted, big changes under DOGE could reduce housing demand in some markets (especially in the VA and DC markets) as we wrote about last week. And that has pulled builder sentiment sharply lower. But other markets should see a nice increase in multifamily activity as this cycle moves from trough into a growth mode.

Third, nonresidential construction is also mixed. We still saw some of the infrastructure spending taking place at a rapid pace, despite some risks from DOGE efforts. And remember, many of these sectors are still experiencing spending levels 3-4 times higher than we saw in 2019 (prior to the pandemic). Some of this is the impact of inflation, but much of it is continued demand that remains near historical levels.

It might be a broken record, but the manufacturing sector is still clipping along at more than $235 billion in spending (vs. $80 billion annual average in 2019). Although the rate of growth has slowed from an average growth rate of 57% across 2024 to 5.7% in the January report (in other words, against tough comparisons), total spending volumes are still strong.

We see this in many sectors. Now, for those businesses that are setting their 2025 growth rates and budgets based on growth above 2024, then this will feel like a slowdown. But for those that saw material and labor shortages in 2024, and they took on what they could handle based on those limitations, this year will feel similar. - KP

- **Durable Goods New Orders Stronger Than Expected.** There are a lot of conflicting economic reports out there right now (reference the current GDPNow estimate). One of those that gave us very strong signals was the durable goods report from January.

  Overall, new orders for Durable Goods were very strong in January. Granted, much of this would have been collected prior to the start of the Trump Administration and clarity on tariff risk. Not that it should impact overall orders, but there are some industries that build dealer or showroom inventory that might take a different approach depending on what happens with tariffs in the long run. In other words, some may have pre-loaded orders to get ahead of tariff risk (for those products that have components sourced in other countries, etc.).

  In the January data, when we compare it to January of 2024, there was strong growth across the board except in automotive. That was the only sector down 3.8% Y/Y. But there was a range of new order growth with strong sectors showing up in aerospace (against easy comparisons to a year ago), computers, communications equipment, defense aircraft and parts, nondefense capital goods and even defense capital goods.

Durable Goods Manufacturers' Shipments and New Orders

[Estimates are shown in millions of dollars.]

Item	Monthly			Percent Change	Year to Date		
	Jan 2025 [2]	Dec 2024 [r]	Nov 2024	Dec - Jan [2]	2025	2024	Percent Change 2025/2024
Total:	286,002	277,347	282,318	3.1	263,268	252,522	4.3
Manufacturing with unfilled orders:	207,179	197,071	201,244	5.1	192,809	180,455	6.8
Primary metals:	26,985	26,715	26,896	1.0	27,343	26,801	2.0
Fabricated metal products:	36,658	37,121	36,866	-1.2	35,949	35,329	1.8
Machinery:	37,579	37,519	37,459	0.2	36,804	36,362	1.2
Computers and electronic products:	25,773	25,339	25,234	1.7	22,662	21,935	3.3
Computers and related products:	2,426	2,265	2,297	7.1	2,224	1,960	13.5
Communications equipment:	3,154	3,135	3,080	0.6	2,498	2,271	10.0
Electrical equipment, appliances,	14,874	14,862	14,792	0.1	13,926	13,490	3.2
Transportation equipment:	96,522	87,884	93,012	9.8	82,821	75,022	10.4
Motor vehicles and parts:	59,126	60,652	61,258	-2.5	54,688	56,858	-3.8
Nondefense aircraft and parts:	20,278	10,458	14,712	93.9	14,166	6,376	122.2
Defense aircraft and parts:	5,656	5,548	5,510	1.9	5,018	3,696	35.8
All other durable goods:	47,611	47,907	48,059	-0.6	43,763	43,583	0.4
Capital goods:	104,962	94,855	100,063	10.7	91,475	81,771	11.9
Nondefense capital goods:	90,590	80,262	84,774	12.9	80,576	71,364	12.9
Excluding aircraft:	75,139	74,515	74,365	0.8	71,402	69,834	2.2
Defense capital goods:	14,372	14,593	15,289	-1.5	10,899	10,407	4.7

When we look at the data sequentially, we would also point out the growth in aerospace and how quickly it is recovering. Remember, there are 10,000 or more suppliers tied to that sector which will get a boost with this new rate of orders.

Also note how strong new orders for computers were, fitting nicely into the AI, data center, and automation narrative that we hear so much about. Investments in that sector are certainly supporting that buildout and strong annual growth rates expected.

Remember the ripple effects of this strong new order growth with demand for raw materials, etc. - KP

Global Economic Items

- **Who Benefits from the Trump Assault on the Old Order? –** Any way one cuts it the Trump era will be extremely disruptive and it may be years before anyone can definitively declare who the winners and losers are. To be honest, the global economic situation has been in need of radical restructuring for decades. Critics have pointed out that China's rise has been at the expense of the US, Europe and Japan simply because this was a matter of a command economy competing with market-based systems. Europe has been sliding into mediocrity due to burdensome regulations and barriers that pushed productivity down. Japan has been hampered by an aging population and geopolitical conflict has been constant. The US once played a truly dominant role in the global economy but China has been eroding that position and decades of losing its manufacturing base caught up. Calls for reform have been persistent but rarely acted upon. In a matter of a few weeks the Trump team has attempted to address all of this at once. Will any of this work or will new problems emerge to replace the old ones? Do tariffs rescue the US industrial base or cripple it? Will retreating to isolationism protect the US economy or ruin it? If the US pulls away from its role as "world policeman" will another nation step up or will these conflicts just blaze away on their own? **It is far too early to answer any of these questions but analysts are starting to identify likely winners and losers.**

  Despite all the pressure applied to China many assert that they will emerge as the big winners in the next few years. There are three reasons for this. **The first is that China is truly autocratic state. Decisions on currency value, trade policy, access to capital, interest rates and just about everything else can be made instantly on orders from the leadership**. Trump has been trying to execute these changes as quickly but the US system is not autocratic. This kind of power can be very useful but it can also backfire badly. Look at what happened to the Chinese property market over the last few years. China allowed billions to flow into that market and the building frenzy drove growth until the whole house of cards collapsed. A lack of balance is not a good thing.

  The second advantage is the US pulling away from relationships. The new isolationism is an opportunity for the Chinese to move in. This can also backfire as the US was often exploited by these relationships. On the other hand, China gets preferential access to raw materials as well as market access for Chinese companies.

  The third advantage is that the US will be pulling away from security commitments. Is this the end of Taiwan as an independent entity? Will China move into other Asian regions? Will its military engage in places the US walks away from?

  The bottom line is China sees itself as a rival and one that should be more powerful than the US in every respect. An isolated US with few allies will bolster Chinese ambitions.

Raw Material Items

- **Copper Surges.** There are a lot of moving parts right now in global commodities and how tariffs might affect final prices for products. Of late, copper has become a key focal point because of some challenges on the supply side of things, and the possible impact from tariffs.

The chart below shows the historical price of copper, and we can see that it is approaching new all-time highs (it moved over 5.00 in May of 2024 and closed today at 4.81). This is up 22% year-over-year and is 18.5% higher YTD through March 5th.

There was a mild impact from power outages in Chile that delayed mining production. But much of this surge in price is coming at the hands of speculators trying to weigh the impact of tariffs. As one might expect, the number one copper source for the US is Mexico at $2.68 billion, China at $2.14 billion, and Canada at $1.79 billion. All of them primary targets of tariffs and without exemptions, will push prices for copper products up 20-25% prior to currency adjustments.

Given how critical this is to US manufacturing activity (along with critical military equipment and technology), one might expect to see exemptions to tariffs on copper at some point. Stay tuned. - KP

Consider This: Personal Thoughts and Insights from Chris and Keith

- **Some Animal Observations –** For once dog people do not have to stop reading. I have observations about the canine companions as well as feline. I was at a conference lately that included several service dogs. One was a seeing eye Lab and the other accompanied a woman in a wheelchair. I was struck by their vigilance and dedication to duty but was more impressed by their “recess time”. Their people understood their doggies needed some break time and the dogs reveled in that freedom. The Lab had been longing to get attention from others and bolted to the nearest crowd with a very excited tail. He soaked it up for about ten minutes and then came back to his person. The mixed breed attacked a squeaky toy with determination and convinced several people to throw it for her. The woman in the chair laughed heartily at these antics. The dogs looked just like the kids in school pouring out on the playground.

  As for the kittens, I watched two big, long-haired cats on leashes making their way across the airport. They might have been Maine Coons – they were definitely big enough. Never have I seen an animal comport themselves with more dignity. No pulling on the leash, no deviation from the path. They walked on either side of the older gentleman in perfect lock step. When he sat down, so did they. I remarked on this to him and he said both were 15 and had been his from the start. “They are also very protective” I noticed that both watched me carefully and I heard a low growl when I got close to him. They both had claws that looked more like talons so I kept my distance until I got permission to pet. (The growl changed to a loud purr!)

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Business Cycle Indicators We Are Watching

An Early Warning System for Cycle Changes

We use the following indicators as early warning devices; when they move, it typically signals a change in the current business cycle. We will continue to update these on a weekly basis as new data is available and specific, deeper-dive commentary on these factors will be included in the written portion of the briefing as changes occur.

		Manufacturing				Services			
Country PMI	Trade with US (in billions)	Current Month	Latest Month PMI	Prior Month PMI	M/M Change	Current Month	Latest Month PMI	Prior Month PMI	M/M Change
US		Feb	52.7	51.2	1.5	Feb	51.0	52.9	-1.9
Global PMI	$ 4,700	Feb	50.6	50.1	0.5	Feb	51.6	52.2	-0.6
Canada	$ 665	Feb	47.8	51.6	-3.8	Feb	46.6	49.0	-2.4
Mexico	$ 661	Feb	47.6	49.1	-1.5				
China	$ 655	Feb	50.8	50.1	0.7	Feb	51.4	51.0	0.4
Eurozone PMI	$ 632	Feb	47.6	46.6	1.0	Feb	50.2	50.2	0.0
ASEAN	$ 369	Feb	51.5	50.4	1.1				
Japan	$ 210	Feb	49.0	48.7	0.3	Feb	53.7	53.0	0.7
Germany	$ 201	Feb	46.5	45.0	1.5	Feb	51.1	52.5	-1.4
South Korea	$ 161	Feb	49.9	50.3	-0.4				
UK	$ 118	Feb	46.9	48.3	-1.4	Feb	51.0	50.8	0.2
Taiwan	$ 114	Feb	51.5	51.1	0.4				
India	$ 113	Feb	56.3	57.7	-1.4	Feb	59.0	56.5	2.5
Vietnam	$ 113	Feb	49.2	48.9	0.3				
Netherlands	$ 88	Feb	50.0	48.4	1.6				
Ireland	$ 88	Feb	51.9	51.3	0.6	Feb	53.2	53.4	-0.2
Switzerland	$ 87	Feb	49.6	47.5	2.1				
Italy	$ 83	Feb	47.4	46.3	1.1	Feb	53.0	50.4	2.6
France	$ 80	Feb	45.8	45.0	0.8	Feb	45.3	48.2	-2.9
Brazil	$ 78	Feb	53.0	50.7	2.3	Feb	50.6	47.6	3.0
Singapore	$ 65	Feb	50.7	50.9	-0.2				
Thailand	$ 60	Feb	50.6	49.6	1.0				
Australia	$ 39	Feb	50.4	50.2	0.2	Feb	50.8	51.2	-0.4
Indonesia	$ 37	Feb	53.6	51.9	1.7				
Russia	$ 36	Feb	50.2	53.1	-2.9	Feb	50.5	54.6	-4.1
Spain	$ 35	Feb	49.7	50.9	-1.2	Feb	56.2	54.9	1.3
Hong Kong	$ 34	Feb	49.0	51.0	-2.0				
Philippines	$ 23	Feb	51.0	52.3	-1.3				
Poland	$ 11	Feb	50.6	48.8	1.8				
Greece	$ 3	Feb	52.6	52.8	-0.2				

Sources: S&P Global, Caixin, JP Morgan, Jibun Bank, Nevi, BME, CIPS

Forecast

Real GDP

2019	2.3%
……..	
2023	2.1%
2024 (Est)	2.8%
2025 (Est)	2.5%

Private Investment (GPDI)

2019	5.2%
……..	
2023	2.1%
2024 (Est)	3.4%
2025 (Est)	4.5%

Business Investment

2019	-0.1%
……..	
2023	4.0%
2024 (Est)	2.0%
2025 (Est)	2.5%

Retail Sales

2019	3.0%
……..	
2023	2.5%
2024 (Est)	3.5%
2025 (Est)	3.5%

New Housing Starts

2019	1.3M
……..	
2023	1.1M
2024 (Est)	1.2M
2025 (Est)	1.4M

Auto Sales (Annual)

2019	16.9M
……..	
2023	15.1M
2024 (Est)	16.1M
2025 (Est)	16.0M