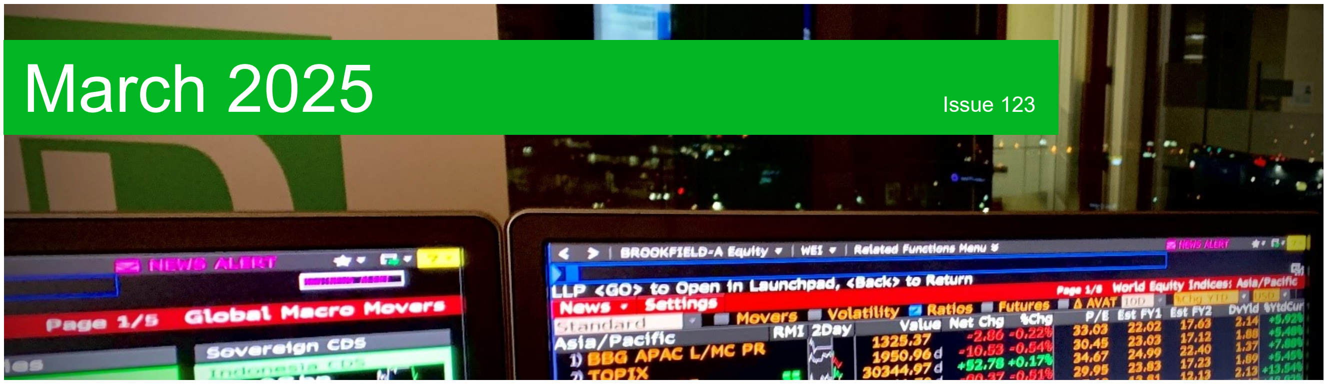
The Charter Group Monthly Letter



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Economic & Market Update

Tariffs Didn't Make Argentina Great Again

With all the news coverage of tariffs lately, they may seem like a new thing. In reality, tariffs are quite an old thing. And there's a good reason why they haven't been used in North America in living memory: because they don't work as hoped.

If big tariffs were the answer to economic success they would not have gone out of fashion after related experiments in the 1930s.

One of the few countries that have maintained a massive tariff regime since then is Argentina. It is a case study that provides some important lessons.

Fortunately, there is an on-going case study to provide us with this lesson elsewhere. That elsewhere is Argentina where your portfolio manager spent some time at the beginning of February.

Now, before I get into the rather boring subjects of economics and trade, I would be remiss if I didn't highlight some of the country's features that make it a wonderful place to visit. Argentina is known for its red wines and steak in the north (where cattle predominates) and lamb in the south (where it is mostly sheep herding).

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The splendor of Buenos Aires is revealed in French-inspired architecture dating back to the city's heyday in the late 19th century through to the early 20th century (hint: that was before tariffs were widely implemented 😊).

Finally, the mountainous terrain in the Patagonian Andes rivals the Canadian Rockies, but with unique formations that are not seen in North America.

If they had ever built the long-promised Pan American Highway all the way to Tierra del Fuego (as far south as one can get excluding Antarctica), I would imagine that there would have been traffic jams of intrepid North Americans driving to visit Argentina. Instead, because of economic priorities that focus on things other than tourism, sightings of North Americans are relatively rare (European visitors are a little more common because of language and more family connections).

Beginning in the 1890s, in an era of *different* economic priorities, Argentina rose to the top tier in terms of wealth per capita and maintained that status for about three decades. During this time, European émigrés would often be keener to head to Argentina than to North America. Much of the country's wealth came from the establishment of Buenos Aires as the primary port city for the Spanish colonies in Latin America. Trade finance and banking developed there because of this. Then, Argentina, with its considerable endowment of fertile land, became a major player in agriculture, adding further to wealth.

Then, political instability erupted in 1930 and, arguably, it has persisted all the way through to the current day. Campaigning for economic independence from foreigners was an effective way of justifying military coups (in 1930, 1943, 1955, 1962, 1966, 1976, and 1981) or for winning occasional elections in the intervening periods.

As Argentina stumbled economically relative to its halcyon period from 1890 to the late 1920s, political instability and populism emerged.

This provided the environment to propose protectionism in an attempt to get back to the country's glory days.

The idea of manufacturing everything in the country while eschewing international trade had a seductive appeal. The politics of this wasn't so much left versus right. Instead, it was a kind of Argentine populism. And any leader deviating from that didn't last long.

And, if you're going to manufacture everything domestically, you are going to need tariffs so that more efficient producers elsewhere in the world don't come in and undercut you.

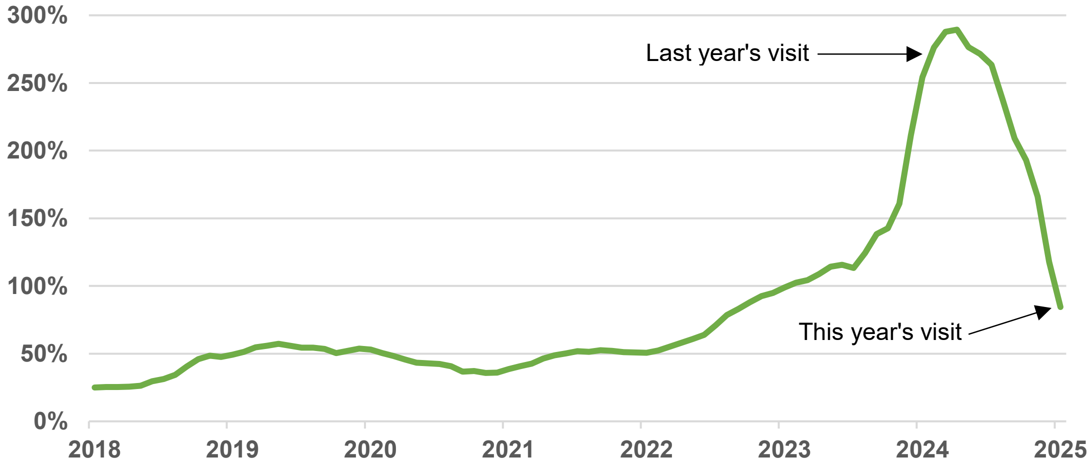
Well, Argentina is no longer in the top strata of the world's wealthiest countries. It now hovers around 70th place, battling it out with its neighbours Chile and Brazil.

For fairly obvious reasons, protectionism is not a recipe for success with all the economic disruption it can yield. During my previous visit a year ago, annual inflation was 254%. This time it was 84% (**Chart 1**). Much of this inflation is the result of printing money. The spectre of debt default due to a lack of tax revenues because of weak growth is also a contributor. But an element of inflation also results from the tariffs. While there is an effort to manufacture as much as possible domestically, Argentina is just not able to produce all the necessities, and especially not the luxuries, demanded by the population. If people want something that is not produced in the country, they are going to need to pay extra because of the tariff-induced higher price.

Instead, the country has mostly been in a perpetual state of inflation, slow economic growth, and debt default. Arguably, tariffs have had a role to play in all these aspects.

Chart 1:

Annual Inflation Rate for Argentina



Source: Bloomberg L.P. as of March 7, 2025

In December 2023, Argentines elected a new government that actually promised spending cuts. Eventually, when inflation becomes high enough, tough medicine policies can look more compelling despite Argentina's historical aversion to them!

A new government was elected in late 2023 to tackle inflation, economic growth, and the debt problems.

The focus has been on spending cuts.

So, what are the prospects that after almost 100 years that Argentina will reclaim its economic glory? It's too hard to tell at this point. The effects of ambitious policies can take some time to be fully realized. As noted, there has been some progress already on inflation (although it is still very high by our standards). Also, the Argentine peso has strengthened (I noticed this by going to the same McDonald's location as the year before and the price of a regular Big Mac Meal rose from $6.67 to $14.26 on my Visa statement!!).

Notably, the long-standing tariffs have remained in place.

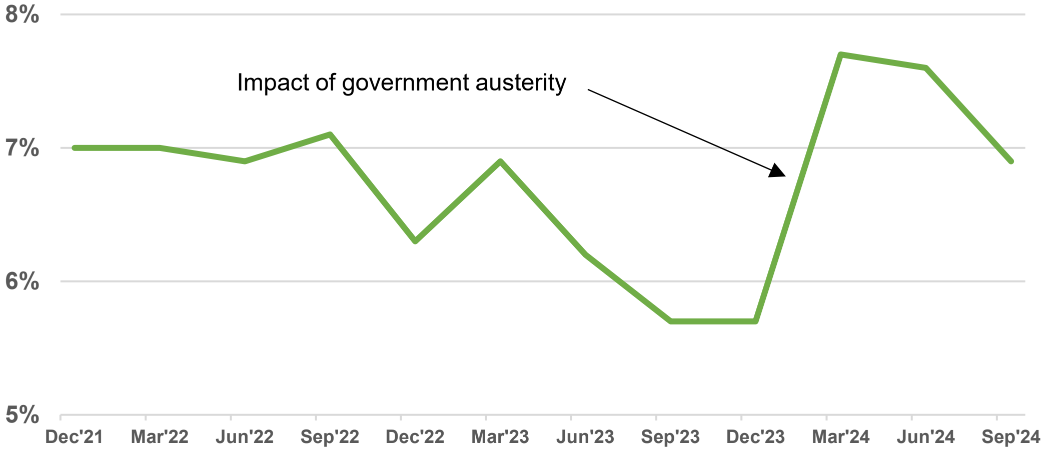
Some progress has been made.

Austerity has hit Argentine household budgets hard. Even though inflation has come down some, unemployment has jumped over the past year (**Chart 2**). Voter patience with fiscal reform won't last forever. This is, after all, a country that has defaulted nine times since

But will tariffs and voter impatience derail things?

they gained their independence as governments have continually acceded to the demands from the population for handouts and subsidized employment.

Chart 2:
Unemployment Rate for Argentina



Source: Bloomberg L.P. as of March 7, 2025

Tariffs can also lead to trade wars. With the U.S. now threatening reciprocal tariffs against almost everyone, will Argentina suffer consequences?

And, amazingly, despite having some of the highest tariffs on imported American goods, this has yet to capture much attention from President Trump. In addition to inflation and sluggish growth, tariffs have had a notable history of causing some nasty trade wars.

Chart 3:
Tariffs in Argentina Compared with Canada

Source: Bloomberg L.P. and The World Bank as of March 7, 2025

The bottom line is that tariffs can initially be a winning political issue, but, on net, they are almost always a losing economic proposition. Argentina's failure in making any sustained progress back to its former preeminence is compelling evidence.

Model Portfolio Update[1]

The Charter Group Balanced Portfolio
(A Pension-Style Portfolio)

	Target Allocation %	Change
Equities:		
Canadian Equities	12.0	None
U.S. Equities	38.0	None
International Equities	8.0	None
Fixed Income:		
Canadian Bonds	22.0	None
U.S. Bonds	6.0	None
Alternative Investments:		
Gold	8.0	None
Silver	1.0	None
Commodities & Agriculture	3.0	None
Cash	2.0	None

No changes were made to the asset allocations or the specific holdings in the model portfolios since January.

No changes to the asset allocations or the individual securities in the model portfolios since January.

The big gainers during February were gold, international stocks, and bonds. Gold was up as investors looked to hedge against the potential inflationary effects of tariffs. Bonds were higher as yields fell in anticipation of slowing economic growth due to tariffs. And European stocks were higher on the realization that European countries may have to rebuild their military defenses if they are forced to navigate the new geopolitical world with less help from the U.S.

Gold, bonds, and international stocks in general were the positive contributors to results.

These factors were enough to tilt the portfolios slightly to the positive for the month despite the concerns with all the tariff threats.

[1] The asset allocation represents the current *target* asset allocation of the Balanced Model Portfolio as of March 7, 2025. The asset allocations of individual clients invested in this Portfolio may differ because of the relative performance of the asset classes since the last rebalancing and because of differences in the timing of deposits and withdrawals. The Balanced Model Portfolio is part of a sequence of five portfolios ranging from conservative to aggressive: Conservative, Balanced Income, Balanced, Balanced Growth, and Growth.

So, what about the tariffs? As discussed in the first section of this newsletter, they rarely work as intended. The question is whether Americans will be quicker to respond negatively to tariffs than Argentines by shifting future voting intentions. The answer could be yes. Numerous opinion polls indicate that Americans were already growing concerned about inflation and employment before the U.S. elections in November. And investors have already thrown a few tantrums recently. For a president who referenced the performance of the stock market repeatedly in his first term, perhaps this was the impetus for the recent delays and selective reversals in tariff policies over the last few weeks.

Will Americans have the patience to tolerate higher prices and employment risks resulting from tariffs?

Or will tariffs become too politically risky not to be significantly modified or repealed?

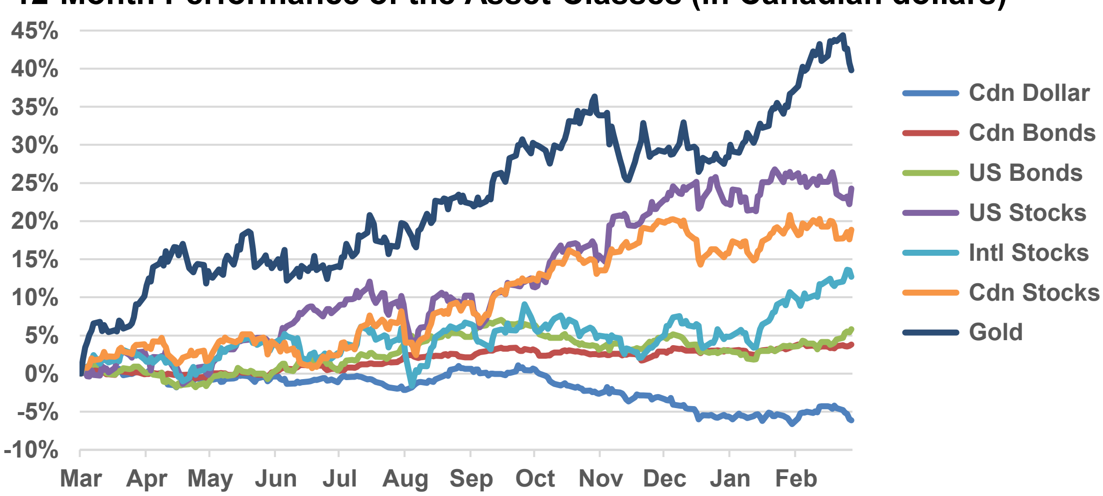
If there is modification or a reduction in tariffs, equity investors could find reason to become more bullish.

As discussed in *The Charter Group Monthly Letter's* February issue, Americans have not shown much tolerance for relatively minor inconveniences. To maintain presidential popularity, the White House might have to make more modifications depending on industry and country. In the case of Canada, relative to Mexico and China, it is challenging to come up with convincing reasons as to why Americans should endure higher costs and lower economic growth. If upset investors are able to get the U.S. to back off on some or most of the tariffs, it would be reasonable to expect equity markets to respond favourably.

Below is the 12-month performance of the asset classes that we have used in the construction of The Charter Group's model portfolios. (**Chart 4**).[2]

Chart 4:

12-Month Performance of the Asset Classes (in Canadian dollars)



Source: Bloomberg Finance L.P. for the interval from March 1, 2024 to February 28, 2025

[2] Source: Bloomberg Finance L.P. – The Canadian dollar rate is the CAD/USD cross rate which is the amount of Canadian dollars per one U.S. dollar; Canadian bonds are represented by the current 3-year Government of Canada Bond; US bonds are represented by Barclays US Aggregate Bond Index; U.S. stocks are represented by the S&P 500 Index; International stocks are represented by the MSCI EAFE Index; Canadian stocks are represented by the S&P/TSX 60 Composite Index; Gold is represented by the Gold to US Dollar spot price.

Top Investment Issues[3]

Issue	Importance	Potential Impact
1. Global Geopolitics	Significant	Negative
2. Inflation (Portfolio Impact)	Moderate	Positive
3. China's Economic Growth	Moderate	Negative
4. Canadian Federal Economic Policy	Moderate	Negative
5. Canadian Dollar Decline	Moderate	Positive
6. Global Trade Wars	Moderate	Negative
7. Long-term U.S. Interest Rates	Moderate	Negative
8. Short-term U.S. Interest Rates	Medium	Negative
9. U.S. Fiscal Spending Stimulus	Medium	Positive
10. Canada's Economic Growth	Light	Positive

[3] This is a list of the issues that we currently deem to be the ten most important with respect to the potential impact on our model portfolios over the next 12 months. This is only a ranking of importance and potential impact and *not* an explicit forecast. The list is to illustrate where our attention is focused at the present time. If you would like an in-depth discussion as to the potential magnitude and direction of the issues potentially affecting the model portfolios, I encourage you to email me at mark.jasayko@td.com or call me directly on my mobile at 778-995-8872.

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Accountability is further enhanced by the fact that we commit our own investable wealth to the same model portfolios in which our clients are invested.

The information contained herein is current as of March 7, 2025.

The information contained herein has been provided by Mark Jasayko, Senior Portfolio Manager and Senior Investment Advisor, TD Wealth Private Investment Advice, and is for information purposes only. The information has been drawn from sources believed to be reliable. Graphs and charts are used for illustrative purposes only and do not reflect future values or future performance of any investment. The information does not provide financial, legal, tax or investment advice. Particular investment, tax, or trading strategies should be evaluated relative to each individual's objectives and risk tolerance.

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Index returns are shown for comparative purposes only. Indices are unmanaged and their returns do not include any sales charges or fees as such costs would lower performance. It is not possible to invest directly in an index.

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Thank you from The Charter Group at TD Wealth

Thank you to our clients and community for voting The Charter Group, your favorite for Investment Management and Financial Planning in Langley for the <u>fifth</u> year in a row.

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