GDS Investments

Client Note, April 2025

> *"So that the record of history is absolutely crystal clear. That there is no alternative way, so far discovered, of improving the lot of the ordinary people that can hold a candle to the productive activities that are unleashed by a free enterprise system."* –Milton Friedman

What a month.

Where shall we start? Market circumstances have changed dramatically even just since our last letter, so let's begin by taking a closer look at some recent economic events and unpacking their financial, political, and humanitarian fallout.

At the top of the list would be President Trump's newly announced package of global tariffs. Trump had already been toying with on-again, off-again tariffs in the first six weeks of his administration. His subsequent April 2 announcement confirms his commitment to tariffs as a vehicle for economic policy and his administration's specific economic vision.

They are not, however, being received well by the market. "President Trump's mindless tariffs will cause economic havoc," says The Economist. "US stocks plunge on fears of economic hit from tariffs; slump in U.S. dollar is 'vote of no confidence in Trump,'" writes The Financial Times. "Trump is about to bet the economy on a theory that makes no sense," declares The New York Times.

It's clear the market was hoping that Trump's riskier economic ideas, voiced during his campaign, were just ploys for votes and not something he intended to do. But Trump 2.0 has shown less responsiveness to market indicators and a greater personal commitment to economically damaging ideas than anyone expected. The market digested this reality by losing nearly 12% of its value in just the first five days following the announcement.

Why has the Trump Administration pursued this unpopular policy so ardently?

If we understand correctly, the main point of the new tariff policy seems to be to "correct" for trade imbalances. "When you look at the trade deficit we have with certain countries ... with China, it's a trillion dollars," President Trump said after announcing his tariff plans. "And we have to solve our trade deficit with China."

Let's be clear that almost this entire conversation is rooted in misunderstanding and, at best, flawed math. First, it's true that there's a trade deficit; the U.S. imports $462 billion in goods from China while exporting only about $200 billion. But that is neither (1) a trillion-dollar imbalance nor (2) bad. "A trade deficit sounds bad, but it is neither good nor bad," writes Tarek Alexander Hassan, an economist at Boston University. He explains:

"A trade deficit can only arise if foreigners invest more in the United States than Americans invest abroad. In other words, a country can only have a trade deficit if it also has an equally sized investment surplus. The United States is able to sustain a large trade deficit because so many foreigners are eager to invest here."

Plus, let's not ignore the difference between trade in goods versus trade in services. Even in places where the U.S. has a trade deficit in goods, it often has a surplus in services, especially technology services.

Ultimately, the formula for determining the tariff rates appears to be fundamentally flawed or even outright manipulated. We won't belabor this point here, but this analysis from the American Enterprise Institute is worth reading. Its authors suggest that actual tariffs, were they to be calculated correctly according to President Trump's stated intentions, should be much lower. The White House math grossly inflates the actual tariffs other countries charge us. As a result, the announced tariffs, built off those inflated numbers, are disconnected from reality, in some cases dramatically so.

The other stated "advantage" to tariffs is that they will bring in more income, giving Congress the ability to fund desired tax cuts. The problem is that tariffs, as they get passed on to the consumer, are themselves effectively a sales tax.

"Tariffs are a tax on imported foreign goods and services," writes the Economic Policy Institute. "Importers who pay the tax initially will typically raise prices to pass this additional cost along to consumers, known as 'price pass-through.' [S]ubstantial research convincingly demonstrates that it is U.S. households who ultimately pay for tariffs."

In this sense, we're simply exchanging one tax for another. So, if these tariffs fail to either correct trade imbalances or reduce the burden on taxpayers, what do they do?

What we've said many, many, many times before: they will ultimately raise costs for consumers and businesses and slow growth in the economy.

Worse, tariffs increase the cost of doing business in a way that businesses can't mitigate easily or quickly. Even if business can increase domestic production, today's globalized businesses have worldwide supply chains that, like it or not, are deeply intertwined and

often formalized into enforceable trade agreements. As a practical matter, reallocating capacity is an effort measured in years. It's not a button corporate America can just push.

President Trump's Announced Tariffs

April 2, 2025

Country	Tariff (Announced)	Tariff (Corrected)	Country	Tariff (Announced)	Tariff (Corrected)
Lesotho	50%	13.2%	Algeria	30%	10.0%
Cambodia	49%	13.0%	Nauru	30%	10.0%
Laos	48%	12.7%	South Africa	30%	10.0%
Madagascar	47%	12.4%	Pakistan	29%	10.0%
Vietnam	46%	12.2%	Tunisia	28%	10.0%
Myanmar (Burma)	44%	11.6%	Kazakhstan	27%	10.0%
Sri Lanka	44%	11.6%	**India**	**26%**	**10.0%**
Falkland Islands	41%	10.8%	South Korea	25%	10.0%
Syria	41%	10.8%	Brunei	24%	10.0%
Mauritius	40%	10.6%	**Japan**	**24%**	**10.0%**
Iraq	39%	10.3%	Malaysia	24%	10.0%
Guyana	38%	10.1%	Vanuatu	22%	10.0%
Bangladesh	37%	10.0%	Cote d'Ivoire	21%	10.0%
Botswana	37%	10.0%	Namibia	21%	10.0%
Liechtenstein	37%	10.0%	**European Union**	**20%**	**10.0%**
Serbia	37%	10.0%	Jordan	20%	10.0%
Thailand	36%	10.0%	Nicaragua	18%	10.0%
Bosnia and Herzegovina	35%	10.0%	Zimbabwe	18%	10.0%
China	**34%**	**10.0%**	Israel	17%	10.0%
North Macedonia	33%	10.0%	Malawi	17%	10.0%
Angola	32%	10.0%	Philippines	17%	10.0%
Fiji	32%	10.0%	Zambia	17%	10.0%
Indonesia	32%	10.0%	Mozambique	16%	10.0%
Taiwan	**32%**	**10.0%**	Norway	15%	10.0%
Libya	31%	10.0%	Venezuela	15%	10.0%
Moldova	31%	10.0%	Nigeria	14%	10.0%
Switzerland	31%	10.0%	Chad	13%	10.0%

Source: The American Enterprise Institute

https://www.aei.org/economics/president-trumps-tariff-formula-makes-no-economic-sense-its-also-based-on-an-error/

This tax will hit consumers of companies that are less affected by the tariffs too. Consider the auto industry. Ford Motor Co. (**NYQ: F**) assembles 80% of the vehicles it sells in the U.S. domestically. By contrast, foreign auto makers like Mazda, Volvo, and Volkswagen are on the opposite end of the spectrum, manufacturing fewer than a fifth of their American sales in-country.

That puts Ford at a major competitive advantage (*note: GDS Investments does not hold a position in Ford*). They should be (relatively) insulated from the impact of tariffs, while their competitors' cost structures just shot up by 25% or more. Wouldn't it make financial sense for Ford to increase prices at least a little? They could increase by 10% to 15% and *still* undercut competitors by a healthy margin. In the short term, Ford has responded to tariffs by announcing lower prices…but only through June 2. This action is less of a commitment to lower prices than a special sale.

In the long run, even Ford is likely to raise prices. "The cost of vehicles will go up. It's just math. The bottom line is there is absolutely no vehicle that won't be impacted by tariffs," former Ford CEO Mark Fields told CNN.

The *way* these tariffs are being implemented is nearly as burdensome as the actual tariffs themselves. Remember, businesses deal in multi-year increments; major decisions today are often intended to pay off months or years from now. But this president is dealing with increments measured in days or even, sometimes, hours. It's possible the newly proposed tariff regime won't last; in just the first month of his administration, the Trump Administration reversed course at least a dozen times. This situation may follow suit.

That would be good, but what business leaders ultimately want is a level of certainty that will allow them to open their checkbooks and invest with a level of confidence that any economic policy implemented today will be in place next month, next quarter, next year. JPMorgan Chase (**NYQ: JPM**) CEO Jamie Dimon said it plainly last month: "Uncertainty is not a good thing." As things stand, business leaders can't even know if some policies will still be in place by the end of the day. That makes long-term investments harder to justify, which by itself will slow growth.

Ultimately, we seem to be heading toward a new protectionist Smoot-Hawley framework, but Smoot-Hawley was a failure even a century ago, worsening the effects of the Great Depression. Indeed, the dreaded words recession and "stagflation" enter the conversation here: rising costs, slowing growth. And to do this after such a long period of impressive growth doesn't make much sense.

The other part that doesn't make sense: alienating the whole world.

International trading partners like China and the European Union are already discussing or implementing retaliatory measures, but here, it's not just tariffs at play. The Trump Administration is clearly experimenting with upending the entire post-World War II international order, and it's making the whole world uneasy.

The post-World War II order—the one largely architected by the United States itself—may not be perfect, but it has given our nation a leading seat at the table and, with it, an enormous amount of influence over all kinds of different policies globally. Losing that influence makes us more vulnerable over the long-term to global political and military shocks without a credible, rooted alliance on which we can lean in moments of need.

This is an important point: power is about more than military might and economic wealth. One of the U.S.'s greatest sources of strength is its soft power, its ability to influence political policy and navigate crises across the world through its relationships, aid programs, military partnerships, and—historically—a relatively open approach to global commerce.

President Trump, unfortunately, seems blind to the very idea of soft power. His administration has shown little interest in preserving this world order or even maintaining long-standing international relationships. It is shocking to us, for example, to hear talk of colonizing some of our closest allies, like Canada, and often doing so in demeaning language, like referring to then Canadian Prime Minister Justin Trudeau as "governor."

At the end of the day, we've taken trust and stability as assets that took generations to build and betrayed that trust. We cannot even begin to predict the consequences to that. We would prefer not to live in a world where people don't trust the U.S., don't feel comfortable visiting our beautiful country, or feel they must develop their own nuclear weapons because they no longer believe they can rely on us when it matters. We simply cannot believe that 77.3 million people voted for an entirely new world order.

And that's just our foreign allies. What about our own people?

It's just as shocking to see DOGE's callousness and carelessness in its own efforts. Immediately cutting funding for cancer treatments for kindergarteners? Putting critical services like social security at risk and reducing services for veterans (people who have risked their lives for the rest of us)? And so much more.

"Musk has been wielding a sledgehammer and tearing down existing structures with little thought for what could replace them," writes Linda J. Bilmes, the Daniel Patrick Moynihan Senior Lecturer in Public Policy at the Harvard Kennedy School of Government. "A more strategic approach could have transformed DOGE into a force for genuine reform."

We agree with the idea of the government operating at higher levels of efficiency, and there's no doubt there is waste in government ripe for trimming and real reform. If nothing else, it's sensible to take a fresh look at whether different government programs are still adhering to their core mandates in a way that respects taxpayer dollars.

Indeed, we would be far more likely to accept DOGE's mission, *if* it were executed with a level of humanity and dignity. Instead, Elon Musk and DOGE have taken a chainsaw both metaphorical and literal to whatever he sees as wasteful. In doing so, however, he and his DOGE team are incurring long-term costs for short-term gains and, in the process, hurting real people.

Ultimately, not everything is a pure economic exercise, and we should not ignore the human impact of these actions, at home or abroad. Can we not pursue efficiency and diplomacy with a level of dignity and respect for the individuals, families, and communities impacted by our changes?

Now, to return to the economics of it all: what does all this mean for the investments we are making at this time?

Despite the enormity and breathtaking extent of changes taking place in Washington, we hold fast to our longstanding view that things are never as good nor as bad as they seem.

Even economic downturns, as devastating as they can be, can also potentially serve as crucibles of opportunity. Notably, famed value investor Warren Buffett is the only billionaire to grow his wealth year to date in 2025, adding $12.7B, even as other billionaires—Bill Gates, Mark Zuckerberg, Jeff Bezos, Elon Musk—have lost billions of dollars so far this year. There are—and will continue to be—opportunities to leverage for the value-oriented.

First, we remain committed to our positions in Google/Alphabet (**NSQ: GOOG**) and Amazon (**NSQ: AMZN**). Even before all the market madness, we already had an affinity for capital-light businesses, which are relatively less vulnerable to tariffs than the heavy industrial portions of the economy. While Amazon and Google will face secondary impacts (e.g., weakening consumer demand in a recessionary environment), they operate under models that can squeeze out efficiency and reward innovations that can help lower prices for consumers. Everyone will be impacted, but we are comfortable with where Amazon and Google remain within a long-term framework.

We are also holding onto a series of new oil and gas investments we discussed in our previous letter: Tidewater (**NYQ: TDW**), Valaris (**NYQ: VAL**), and Schlumberger NV (**NYQ: SLB**). We see a capital cycle at in play with our new acquisitions positioned favorably compared to some of their chief competitors. Shell (**NYS: SHEL**), for example, was a major

threat in previous cycles but has since redirected capex that would have gone to offshore drilling into domestic production. Unfortunately, a lot of those domestic fields just aren't what they once were, leaving Shell looking like a depleting asset. Of our new acquisitions, two have gone through significant restructuring of their balance sheets, improving their competitive posture. They're in a typically deep downturn from a cyclical standpoint, but they are poised to do disproportionately well when the cycle returns.

It may also be worth noting our small, pre-existing position with electric vehicle maker Rivian Automotive Inc. (**NSQ: RIVN**), given Tesla's (**NSQ: TSLA**) plummeting value. Rivian offers an ideal scenario in which all production is domestic. The owner, R.J. Scaringe, is a shrewd leader who thinks long-term, and the company offers an attractive balance sheet. They also have a partnership with Volkswagen to develop "next generation software-defined vehicle (SDV) platforms" to be used in vehicles made by both companies.

Rivian is well positioned here, offering a good tech-stack built internally. In fact, they are almost as much of a 'car operating system' company as they are a traditional auto manufacturer. They are in a great spot to pick up some of the customers Tesla seems to be bleeding. Certainly, Rivian has a customer base fanatical about its product and willing to sing its praises. They are not making money quite yet, but their upcoming 2026 R2 car model shows real promise. In fact, we suspect it may turn out to be a gamechanger, debuting at nearly half the price (starting around $45,000) as Rivian's other, high-end models and competitive with Tesla's lower tier models.

Our one new position is wine and beer maker Constellation Brands (**NYQ: STZ**). They will get caught up in the tariffs, but it's an extremely well-run company that sells a product that has historically been recession resistant. In other words, they produce a consumer staple that traditionally goes up in times of uncertainty. Interestingly, Berkshire Hathaway disclosed—*after* our own acquisition—that they had also purchased over $1B of stock in Constellation, which we regard as validation of our own evaluation of the position.

In closing, even after everything, we remain cautiously optimistic.

No doubt we have yet to face the worst fallout from White House decisions that have already been made, much less future decisions. Worse, as the economy weakens and individual households are hit harder, the potential for civil unrest rises. We hold no illusions that we've seen the worst of bad economic or political policy.

But we cannot help but think that President Trump is overplaying his hand to his own detriment, given that his electoral victory hinged not on tariffs, culture war politics (e.g., "men in women's sports"), or forcibly annexing territory (talk of annexing Canada didn't even come up until after the election!) but rather on immigration reform and lower prices.

Consequently, we are skeptical of just how far or how long this kind of decision-making can hold out. If nothing else, bad economics likely means a voter backlash in the 2026 midterm elections. We are already seeing early signs of this. Here in Pennsylvania, a Democrat won a special election in an R+23 district. Even in the recent Florida congressional races, where Republicans still won, the election results show 25-point movement in favor of the democratic nominee. If that pattern holds in future elections in districts less solidly red than FL-01 and FL-06, Republicans could fare poorly in the 2026 midterm elections. They certainly seem worried about a potential "midterms wipeout."

That worry may well translate—hopefully sooner rather than later—into more sensible and grounded policies better designed to benefit everybody and refocused into areas that could genuinely support the private sector. For example, rather than focusing on tariffs, the Trump Administration could shift to working on deregulation in areas where excessive red tape hinders the ability to businesses to hire, expand, and grow. That is certainly our hope, at any rate.

Regardless, equity markets may well be at a major inflection point that will determine success or failure over the next decade, not unlike the late 90s or 2008. In this environment, those investors who have the patience, conviction, and emotional intelligence to resist panic-driven behavior and to own what is currently out of favor should be handsomely rewarded in time—just as they were after those other downturns.

With warm regards,

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