



Wealth Management
Dominion Securities

Cooper Wealth Management of
RBC Dominion Securities



Thoughts on the market

March 24, 2025

RBC Dominion Securities Inc.

Our Advisors

Trevor Cooper

Portfolio Manager &
Senior Wealth Advisor

Walter Harmidarow

Portfolio Manager &
Senior Wealth Advisor

Charles Cook

Portfolio Manager &
Senior Wealth Advisor

W. Frank Cooper

Senior Wealth Advisor

Rachel Cooper

Associate Advisor

Jeff Gray

Associate Portfolio Manager

Amanda DeGroot

Financial Planner & Associate
Advisor

Our Team

Pamela Townsend

Karen Charlesworth

Holly Kelly

Stephanie Fletcher

Maddy Bodden

Erica Vukovich

March Madness



“Well, I never heard it before, but it sounds
uncommon nonsense.”

- Alice in Wonderland

When we normally talk about March Madness, we are usually referring to the annual NCAA Men’s and Women’s Basketball Tournaments. This year, the broad and sweeping changes of the Trump administration are the main topic of conversation both in Canada and around the world, particularly when it comes to tariffs. Given the level of concern about their possible impact, we will address the challenges posed by tariffs and the current US administration in general and discuss how we are positioning our portfolios to best defend against further unexpected developments.

Let's start with the big issue first: the 25% tariff on all goods coming from Canada. Normally, tariffs must be approved by both the House of Representatives and the Senate. The President can only use an Executive Order to impose tariffs for the sake of national security, which is why he made the tariffs about fentanyl and border security. Last year, 43 pounds of fentanyl was caught at the Canadian border versus 21,100 pounds from Mexico. The illegal immigration has a similar ratio. So why is Canada being treated like Mexico? Here are some possible explanations.

The most popular theory is that they are trying to raise their revenue so they can push through more tax cuts. Given their record deficits and spending plans, this is not a surprise and could be a barrier to a reasonable settlement. Next most likely is an early renegotiation of the USMCA free trade agreement, similar to what the President did in his first term. This is a significant bargaining chip that Canada and Mexico have, which could further delay tariffs being imposed. Finally, the President has also made it clear that he wants manufacturers to return to the US, which is why we are halfway through the latest reprieve from tariffs. Manufacturers have been told they can avoid tariffs by relocating. That is simply not viable. The auto industry has fully integrated their supply chain into Canada and Mexico, both now under tariff threat. China could be an alternative, but their tariffs are even higher, and Europe simply doesn't have the capacity. Automakers can simply pass the cost on to consumers, who would be paying higher prices anyway either through tariffs or less price efficient new US manufacturing. These relationships took years to develop and can't be broken because the President says so. The car companies can't afford to spend billions building new plants and tariffs would effectively destroy their business model. Further, with US unemployment at 4%, and the strict new regulations on immigration, where do they propose to get the necessary skilled workers from? None of these things will reduce inflation, which is a key Trump election promise.

The 25% tariff on steel and aluminum is also puzzling. Canada provides roughly 30% of the aluminum used in the US every year, which can only raise prices. The only other producer that could meet this demand is China, but with their tariffs and shipping costs, this is an even more expensive option. Steel and aluminum plants also take years to build and once again, why would US manufacturers want to pay the higher price?

The Trump administration has also imposed a 10% tariff on Canadian potash. US farmers import 80% of their potash from Canada and the only two other possible sources are Russia and Belarus. Given the extra shipping costs and the current political climate, these are not viable alternatives, which will force US farmers to either absorb or pass on the cost to consumers.

The final tariffs are a 10% charge on Canadian oil and gas. Canada ships more than 4.3 million barrels per day of oil to the US and provides 99% of the natural gas the US imports. Building new domestic infrastructure in the US is possible but Canadian natural gas is a lower cost and more reliable option, particularly as Canadian pipelines into the US are already in place. As natural gas is a primary fuel for electricity production, a tariff would also raise those costs especially in the US Northeast. The US does produce enough natural gas to meet their needs, but they profitably export significant supply to Mexico and the rest of the world with liquified natural gas. With oil, most US refineries are set up to process Canada's heavier oil, which they buy at a discount to the benchmark West Texas Intermediate price, allowing them a wider profit margin. The US then exports their excess supply at the higher global market price. Tariffs would again hurt these profits and

dampen growth of the economy. Unless the US plans to spend billions more on infrastructure, this plan looks like a strict cash grab.

These tariffs seem to be a violation of the USMCA free trade agreement between the US, Canada and Mexico. Given that the tariffs do not appear to make business sense, and if they are not simply a bargaining tool, then the sole motive is to raise government revenues to help combat their growing budget deficit, along with the cost cutting effort of the Department of Government Efficiency. Last year, the US imported \$4.11 trillion of goods and services. If they tariff everything at 25%, they raise just over \$1 trillion. The projected US budget deficit for this year is \$1.9 trillion. To balance the budget, they would have to fire another 108,000 civil servants, who earn an average wage of approximately \$83,000. That is a tall order and combined with higher prices across the economy, they are very unlikely to win many votes at the midterm elections in 2026.

The Republicans managed to get the debt ceiling raised this month with the surprising cooperation of the Democrats, who were more afraid of what the President would do with a closed government. This was an opportunity wasted by the Democrats to finally challenge the White House's actions. The interesting news is that Republicans have been advised not to hold town hall meetings because their people are beginning to protest what the Administration is doing. This overall negative sentiment has been reflected in stock market prices, as the market wants as much certainty as possible.

The tariffs that are receiving the least protest but will have a big effect on US consumers are the 30% tariffs on China. In 2023, China exported \$501.23 billion worth of goods to the US covering everything from raw materials to a huge list of finished goods. While tariffs act as a one-time inflationary lift in prices, the base cost of goods will rise and once again disproportionately impact lower income households. As we have noted before, higher prices don't translate into more votes and the US elected this Administration at least in part on the promise of a lower general price level.

When the news cycle is this noisy, confusion is the result. The key to managing through the noise is to concentrate on the underlying mathematics of the market. There are two key things we need to monitor: the state of the US economy and US corporate earnings. As long as unemployment stays low, the US consumer continues to spend, inflation stays steady, and US gross domestic product continues to grow, the underlying fundamental valuation of the market will remain and eventually be reflected in stock prices. Given the policy chaos out of Washington, we wouldn't be surprised to see some weakness in US GDP as it is difficult for businesses to make long-term investment decisions in this environment. However, if corporate earnings hold up in the current quarter, this will improve overall market conditions.

Our overall portfolio positioning remains defensive. The Canadian dollar investments focus on dividend and defensive names, such as Dollarama, Pembina and Waste Connections. We will be selectively adding in our covered call strategy to enhance income and provide some downside protection. Our goal during this time of uncertainty is to put the cash we have built up to work and invest opportunistically as market opportunities present themselves. Also, we will be using Canadian dollar hedged shares when buying US equities where possible to protect against US dollar fluctuations.

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In conclusion, market downturns, whether caused by political turmoil or a weak economy, tend to be short-lived and represent a buying opportunity. According to data from Hartford Funds, the average bear market, which is a decline of 20% or more from recent highs, has lasted less than 10 months, based on market data going back to 1928. Remember the psychology of the successful investor: in a declining market, you should be considering buying opportunities rather than worry about selling. Worry is a poor use of imagination. Don't be like Alice. Avoid rabbit holes, particularly media created ones. Until next month, stay well.

As always, questions, concerns, comments, and feedback are always welcome.

Yours truly,

Trevor, Walter, Charles, and the Cooper Wealth Management team



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