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Pivot and Protectionism: Unlikely Allies of The Nine Forces Reshaping the U.S. Market Landscape

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From All-Time Highs to a Fed Pivot: The Week in Wall Street

Wall Street entered the third week of August on edge. Signs of strain accumulated early, as **weekly jobless claims climbed** to their highest level in three weeks, while **nonfarm payrolls** fell to their lowest levels, and the **ISM Manufacturing PMI** extended its contraction streak to five straight months.

The weak labor data not only unsettled markets but also had a ripple effect on politics. President Trump, frustrated by what he deemed underperformance, **dismissed the Bureau of Labor Statistics Commissioner**. This move underscored his dissatisfaction and added a layer of political drama to an already fragile economic moment.

However, the week's narrative shifted dramatically in Wyoming, where at the **Jackson Hole Economic Symposium**, Fed Chair Jerome Powell **hinted that the first rate cut could occur as early as September**. His acknowledgement of labor-market weakness, paired with confidence that inflation is cooling, reassured markets that the long-discussed easing cycle was near.

The effect was immediate: on Friday, the **Dow Jones surged 846 points**, while the **S&P 500 climbed 1.5%** and the **Nasdaq advanced 1.9%**. Still, the week as a whole told a more tempered story:

- Dow Jones: **+1.53%**, and **YTD Return of 7.26%**.
- S&P 500: **+0.27%**, and **YTD Return of 9.95%**.
- Nasdaq Composite: **-0.58%**, and **YTD Return of 11.32%**.
- Birling Puerto Rico Stock Index: **+2.78%**, and **YTD Return of 16.93%**.
- Birling U.S. Bank Index: **+1.98%**, and **YTD Return of 23.89%**.

This was more than a week of data releases and central bank speeches. It marked a **turning point in 2025**: as the narrative shifted from rising fears of recession to cautious optimism.



Dow Jones, S&P 500, Nasdaq Composite, Birling Puerto Rico Stock Index & Birling US Bank Index YTD Returns 8.22.25



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The Nine Forces Reshaping the U.S. Market Landscape

1. Federal Reserve Policy: The Pivot at Hand

At Jackson Hole, Powell acknowledged the growing risks to the labor market and the fragile balance between inflation and growth—a markedly more dovish tone than earlier in the year. Markets interpreted his comments as confirmation that the Fed is preparing to ease policy.

According to the **CME FedWatch Tool**, there is now an **84.7% probability of a 25-basis-point cut in September**, with a second cut later in the year still viewed as likely. The first cut would take rates to the 4.00%-4.25% range, still restrictive but palatable.

Powell stopped short of making a formal commitment, but his remarks were explicit.

2. Labor Market: Fragility Behind the Numbers

July's jobs report revealed just **73,000 new positions**, well below expectations and accompanied by downward revisions to prior months. The **unemployment rate climbed to 4.2%**, the highest since 2023, signaling that the once-reliable strength of the labor market is softening.

Weekly **jobless claims rose to 235,000**, the highest since June, suggesting layoffs are spreading more broadly. Powell described this as a “curious balance” — a market neither collapsing nor strong, but showing clear signs of strain.

3. Inflation Pressures: Tariffs as a Wild Card

Inflation remains the Fed's most delicate balancing act. The latest data show that the headline CPI rose to 2.7%, while the core CPI accelerated to 3.1%, its highest level since February. The latest Inflation Nowcasting projects the July PCE at 2.60% and the Core PCE at 2.89%, with the official release scheduled for August 29. These estimates underscore that while headline inflation is edging closer to target, underlying core pressures remain stubbornly above 2%.

Adding to the challenge, Producer Price Index (PPI) inflation surged 0.9% in July, the sharpest monthly increase in three years, bringing the annual PPI rate to 3.3%. This suggests that companies have only partially absorbed rising wholesale costs so far.

Retailers like Walmart and Target illustrate the distortion: everyday low-margin goods have largely been shielded from price hikes, but higher-margin products are increasingly priced up as tariffs filter through supply chains.

4. Yield Curve: A Return to Normalcy

For more than two years, the U.S. Treasury curve was defined by inversion — a signal of caution that has historically preceded recessions. That anomaly has now faded. As of late August, the **2-year yield stands at 3.68%**, while the **10-year yield is around 4.26%**, producing a positive spread of roughly **58 basis points**.

This steepening represents a quiet but significant shift in market psychology: investors no longer see short-term risk as greater than long-term uncertainty.

The implications are twofold:

- For policymakers, the end of the inversion buys credibility. The Fed can cut without fueling panic that a recession is inevitable.
- For investors, a positively sloped curve restores a more traditional playbook: **carry is back**. Investors can lock in long-dated yields with greater confidence, while still using shorter maturities for liquidity management.

In practical terms, this marks a **transition from defensive to opportunity-driven positioning**.

5. Market Rotation: From Growth to Cyclical

Beneath the surface of the indexes, leadership is shifting. **Mega-cap technology — long the engine of this year's rally — stumbled last week.** Microsoft and Nvidia both slipped more than 2%, while Apple finished the week flat, signaling that even dominant AI-driven names are vulnerable when expectations are sky-high. Meanwhile, **cyclicals and value sectors stepped forward.** The **consumer discretionary sector gained nearly 2%**, while the Industrials Sector **rose about 1.6%**, as transportation firms rebounded on stronger freight volumes, and **Financials advanced by 2%**, with regional banks stabilizing. This broadening of leadership mirrors past late-cycle shifts, when investors prepare for slower but ongoing growth.

6. Volatility: Fed, Trade, and Earnings in the Driver's Seat

The **VIX, Wall Street's fear gauge**, closed the week of **August 22 at 14.22**, well below its **August 1 peak of 20.38**. On the surface, this appears to be a calm return to markets, but beneath it lies a story of shifting pressures.

Three forces are increasingly shaping volatility:

- **Federal Reserve signals:** With the September meeting approaching, investors are debating whether Powell delivers a 25- or even 50-basis-point cut.
- **Earnings dispersion:** Tech continues to post strong results, but transportation, retail, and regional banks are showing weakness — driving sharper rotations across sectors.
- **Trade and tariffs:** Fresh tariff proposals and renewed geopolitical frictions with China are adding uncertainty for supply chains and inflation trends.

The decline in the VIX suggests traders are less fearful in the near term, but history shows such sharp retreats often precede renewed turbulence. For investors, the guidance is clear: treat volatility as an opportunity, within a prudent, well-balanced portfolio.

7. Investor Sentiment: Fragile Confidence Beneath Strong Markets

Sentiment among individual investors remains subdued, even as indexes hover near highs. According to the **AAll Investor Sentiment Survey**, the bull-bear spread is negative at -8.4%, meaning more individual investors describe themselves as bearish than bullish. Bullish sentiment itself edged up to about **30.8% as of August 20**, still well below its long-term average.

Institutional sentiment tells a more constructive story. The **NAAIM Exposure Index** shows professional managers remain moderately overweight equities, while the **CNN Fear & Greed Index** sits in neutral territory. This divergence highlights a familiar pattern: retail investors remain cautious even as institutions quietly position for further gains. The data highlights that the current rally rests more on institutional conviction and faith in the Fed than on broad-based confidence. For now, sentiment remains fragile.

8. Tariff Policy: The Unknown Long-Term Effect on the U.S. Economy

Tariffs remain the **structural uncertainty of 2025**. While some U.S. manufacturers benefit, import-heavy industries are grappling with higher costs. History warns us that protectionism carries risks that extend well beyond the sectors it initially targets.

In the **1930s, Herbert Hoover's Smoot-Hawley Tariff Act** raised duties to nearly 60% on dutiable imports. The results were disastrous: **U.S. GDP contracted by roughly 30% between 1929 and 1932**, world trade collapsed by almost 70%, and unemployment surged above 20%. While the Depression had multiple causes, the Smoot-Hawley Tariff Act exacerbated the downturn by provoking global retaliation and significantly reducing exports.

By contrast, the **Trump tariffs of 2018–2019** were far smaller in scope, but still disruptive. Studies show they cut **U.S. GDP by roughly 0.2%**, reduced real incomes by **\$1.4 billion per month**, and cost an

estimated **142,000 full-time jobs**. Unit prices of tariffed goods rose **10–30%**, with most of the increase passed through to consumers, contributing to a mild but measurable manufacturing recession.

The **new wave of Trump tariffs, set to take effect in 2025**, is already beginning to bite.

- A **Goldman Sachs analysis** shows households typically absorb **two-thirds of tariff-related price increases within four months**.
- According to the **Washington Center for Equitable Growth**, tariffs could raise **factory input costs by 2%–4.5%**, particularly affecting steel, autos, and apparel.
- The **Yale Budget Lab** estimates households may face an additional **\$2,400 in costs this year alone**, effectively turning tariffs into a consumption tax.
- **Back-to-school spending** highlights the squeeze: families are budgeting nearly **\$875 per child**, with 72% of parents expecting higher costs, which will lift total expenditures to **\$39.4 billion** this season.
- **Reuters Breakingviews** calculates tariff revenues now account for as much as **2.6% of GDP**, underscoring their growing role as a fiscal tool but also their drag on growth.

The risk today is that persistent tariffs could:

- **Raise input costs** and reignite inflationary pressures, complicating the Fed's pivot to easing.
- **Spark retaliation** from major trading partners, limiting U.S. export growth.
- **Distort corporate investment decisions**, as firms hesitate to commit long-term capital in an unpredictable trade environment.

Whether this era of protectionism results in a **reindustrialization boom** or becomes a **drag on growth** may prove to be one of the defining questions by 2026.

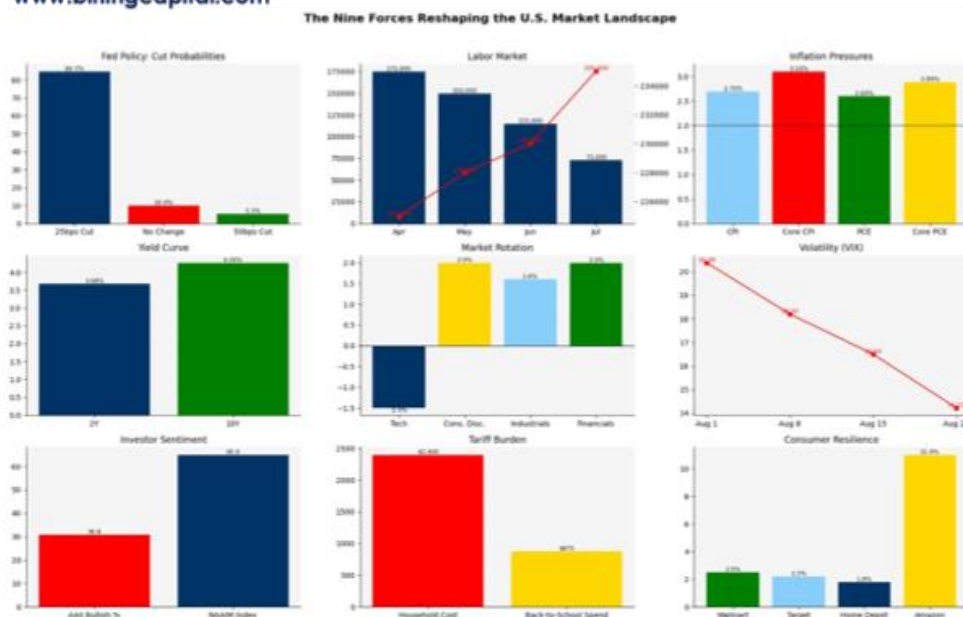
9. Consumer Resilience: The Bright Spot in Uncertain Times

Despite slowing job growth and tariff pressures, the U.S. consumer remains resilient. **Walmart, Target, and Home Depot all reported better-than-expected earnings**, driven by strength in discount goods and home improvement spending. Amazon's North American retail sales grew **11% year-on-year**.

Consumers are trading down, but they are still spending. For now, corporate America is absorbing some tariff-related cost increases and diversifying supply chains. But rising costs in the quarters ahead could test this resilience. The consumer remains the **last line of defense for U.S. growth** — if households falter, the broader economy will follow.



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The Final Word: Navigating the Reset

The current shape of markets is one of **transition, not collapse**. The Fed has signaled a pivot, the labor market is weakening, tariffs are reshaping cost structures, and sector leadership is becoming more diverse. Markets ended the week with a burst of optimism, but beneath the surface, divergence is widening.

After a powerful rally since April 8, it would be unrealistic to expect a straight-line higher. As we approach the traditionally more volatile months of September and October, a few pullbacks should be anticipated.

History reminds us that **two to three meaningful corrections per year are normal**, particularly in periods of uncertainty. Far from being a reason to retreat, these bouts of volatility should be seen as **opportunities to reposition portfolios, diversify holdings, and acquire quality assets at more attractive valuations**.

We enter this phase with **clearer catalysts**: a Federal Reserve preparing to ease, a new tax package aimed at fueling corporate investment, and consumers still resilient despite tariff pressures. In this environment, **equities remain more compelling than bonds**, particularly U.S. large- and mid-caps that balance technology with cyclicals. Sectors that straddle **growth and value — including consumer discretionary, financials, and healthcare — stand out**. In fixed income, **investment-grade bonds in the 7–10 year range** offer both yield and upside as rates fall.

“Markets do not move in straight lines — they reset, they reprice, and they remind us that resilience belongs to those who think strategically. In a world of pivots and protectionism, opportunity belongs not to the impatient, but to the prepared”.



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