DAVIS COMMODITIES LLC

March 2025 Macro Commentary

March was a relatively benign month, but that came to a swift end as President Trump's liberation day tariffs hit on the afternoon of April 2. With the extreme volatility and profitable trades in the program, I have hit the exit on most positions. The thought process has been simply that "discretion is the better part of valor." For now, I am willing to let the dust settle then re-engage. With positioning currently small, there are ample opportunities and lots of dry powder to take advantage.

The positioning in the yield curve was exited as we pushed back to the old high on the spread at +40 basis points(bp). The economic outlook is still quite muddled. Manufacturing data in the US is still weak. Services continue in expansion territory, but edging down toward contraction. On the flip side, job growth continues apace with unemployment still hanging around the relatively tight 4.2%. In order to see the 2/10 widen out over 100 bp, the unemployment data needs to get closer to 5%. The current question that is front and center on the mind of the market is whether or not the new tariff regime will push the US into recession. There is still far too much noise to make any educated guess. Over 50 countries have indicated that they would like to negotiate with some already offering zero tariff. If these negotiations are fruitful, the likelihood of a recession diminishes greatly. Even if a recession is avoided, the current level of tariffs should slow the world economies. While currently flat, a break toward congestion levels near 30 looks like a good place to re-enter the trade.

The other interest rate trade that was exited was the Secured Overnight Financing Rate (SOFR). By Friday, April 4, the market was pricing ~3% Fed Funds. While certainly possible, it was simply a case of too far, too fast. If the US enters a recession, the Fed will act aggressively, but as stated, that is far from a known quantity. In addition, Powell has stated his concern that the tariffs could lead to inflation. The true fear is that the economy stagnates due to the tariffs, but prices increase which forces a wage/price spiral similar to the 1970's. That fear should keep the Fed on hold (barring a shock) for the near term. While I still think that rates will move lower over time, 3% is extreme for now.

The program is still holding a small long Eurocurrency position, but that is being held on a tight leash. The broad defense stimulus being proposed by especially Germany should help to underpin growth and support their weakening industrial base. If that can be pushed through, the euro is not done rallying. However, a failure to juice the manufacturing base through government spending will send it sharply lower. Odds still favor the expansion which is why the trade is still intact. If that possibility gets even slightly less likely, the trade will be jettisoned.

Finally, a quick thought on the current political situation in the US. I sincerely hope you understand that it is never my job or intent to say things are right or wrong. My job is to understand the current and future political and economic climate in order to ascertain where the market will move next. While many talking heads have come forth to offer their opinion of whether Trump's tariff policy is right or wrong, I am simply looking at Trump's stated goals. Unlike his first term, he has not really mentioned the stock market. Instead, he has been quite vocal that he wants lower interest rates, weaker dollar, and lower energy prices. So far, he is batting 1.000. Whether those moves are truly obtained, still remains to be seen.

Sincerely,

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