VISUALIZING MARKET DYNAMICS

A GUIDE TO
MARKET TRENDS

JUNE 2025

June 2025

TODAY'S ECONOMY & "THE MILKSHAKE THEORY"

WRITTEN BY:

Mark Roach
Director,
Small & Micro Cap Equities

Mario Tufano, CFA
Senior Portfolio Manager,
Small Cap Equities

“If you have a milkshake, and I have a milkshake, and I have a straw. There it is, that's the straw, you see? Watch it. Now my straw reaches across the room, and starts to drink your milkshake…”

— Daniel Day-Lewis as Daniel Plainview in There Will Be Blood (2007)

The Dollar Milkshake Theory began making waves on macro podcasts and in finance circles around 2018, nearly a decade into the Federal Reserve’s grand experiment with Quantitative Easing. The premise is simple but counterintuitive: printing more dollars does not necessarily weaken the dollar. In fact, it can strengthen it—thanks to the unique role the United States plays in the global financial system.

In this theory, the world is a giant milkshake of liquidity, the U.S. economy is one of many glasses, and the straw represents the flow of global capital. While traditional economics suggests that increasing supply dilutes value, the Milkshake Theory contends that America’s combination of perceived stability compared to other governments, economic scale, leading innovation, and military strength transforms excess liquidity into gravitational pull. As capital flows back into U.S. markets, it boosts the dollar and keeps borrowing costs low.

From the launch of the first round of quantitative easing in 2008 to the second attempt at quantitative tightening in 2022, the U.S. dollar appreciated nearly 50% despite aggressive money printing and ballooning deficits (see Figure 1). This strength defied conventional expectations. While the Federal Reserve was injecting trillions into the financial system, foreign producers, flush with dollars from U.S. consumers, recycled those earnings into American assets.

The result? “Made in China” often led to “Buy America”—not in goods, but in U.S. financial assets, as surplus dollars were recycled into Treasuries, equities, and real estate. But now, in 2025, the flow of “milkshake” liquidity into the U.S. economy may be reversing—driven by two prevailing forces: DOGE and Tariffs.

Google searches for “tariffs” and “doge” spiked in early 2025 (Figure 2), replacing the fixation on Powell’s Put and the AI arms race that dominated markets last year. The renewed focus on tariffs even sparked curiosity about the 25th president, introducing a new generation to William McKinley and his love of tariffs at the turn of the 20th century.

This public interest in both trade barriers and government reform reflects growing anxiety over the economic fallout. The impact is visible not only in market volatility, but also in the heightened uncertainty with the current course of government policy—levels not seen in over forty years (Figures 3a, 3b,& 3c).

Beneath these two prevailing narratives lie deeper structural fault lines: America’s twin deficits.

- The budget deficit, bloated by stimulus programs and entitlement spending, has averaged nearly 9% of GDP this decade—its highest sustained level since the 1940s (Figure 4b).

- The trade deficit, long overlooked in the name of globalization, has become a focal point for tariff hawks and a proxy for broader concerns over supply chain resilience following COVID.

The budget deficit has its roots in the Federal Reserve Act of 1913, which created the Fed, and the 16th Amendment, which allowed the government to collect income taxes instead of relying on tariffs. This change paved the way for wartime spending, Keynesian stimulus to offset recessions, and ultimately a structural reliance on deficit financing—despite America's longstanding, if aspirational, preference for balanced budgets (Figure 4a).

In contrast, the trade deficit surged after President Nixon's 1972 trip to China, which opened the door to cheap labor and globalized supply chains, fundamentally altering the U.S. economic relationship with the rest of the world.

For decades, this model worked and during the 1980s it turbocharged America's economic engine. The potent combination of cheap labor from globalization, cheap financing as the world eagerly bought U.S. debt, and cheap energy driven by technological advances fueled corporate profit margins (Figure 6).

But that dynamic is shifting. The trade deficit—once tolerated as the price of globalization—is now viewed by many as a strategic vulnerability, exposing critical supply chains and increasing dependence on geopolitical rivals. Meanwhile, the budget deficit—long justified by wartime needs, economic stimulus, and entitlement commitment—is increasingly seen as unsustainable, given the scale of borrowing required to fund persistent spending and the potential inflationary risks that follow.

Today, interest expense consumes nearly 16% of the federal budget, making it the second-largest line item after Social Security (Figure 7a). Nearly half of all outstanding U.S. debt matures within three years and much of it carries rates below current market levels. As refinancing looms, this creates a ticking time bomb for fiscal stability should rates remain at these levels or go higher.

DOGE, now a shadow of its former self without Elon Musk at the helm, is seeking to correct this financial strain. Meanwhile, Trump's "big, beautiful" budget currently moving through Congress threatens to worsen it. Adding to the mix are the Trump Tariffs, aimed at narrowing the trade deficit. All three combined are creating unintended ripple effects that threaten our ability to finance the budget deficit.

Should "Trump 2.0" continue with his policy approach, the U.S. could see tariff levels not seen since the 1940s (Figure 8). This may lead to reduced global trade and fewer surplus dollars recycled into Treasuries. If confidence in the U.S. dollar weakens, the entire milkshake system begins to leak—triggering capital outflows, pressuring the dollar, and driving up borrowing costs.

This is the macro backdrop against which investors are currently operating. Equity markets have rallied from the lows of the year touched during a volatile April and interest rates are still rising instead of falling as they would in times of stress. Gold, on the other hand, is settling in at new highs, signaling a flight to hard assets and challenge to the dollar's role as the world's reserve currency.

In addition, foreign central banks and institutions that once eagerly absorbed U.S. Treasuries are now looking for alternatives. China, for example, has already cut its U.S. debt holdings by more than half since "Trump 1.0" and Russia exited their entire position in 2018. If others follow—and if the Fed does not step in— confidence in the dollar may start to erode and borrowing costs could spike as global markets become flooded with excess supply of U.S. debt.

At the end of the 2007 film There Will Be Blood, oil tycoon Daniel Plainview is seen bowling alone in his mansion when he receives an unwelcome visit from a former preacher who once tried to thwart his land deals. In a now-iconic scene, Daniel delivers a fiery monologue, shouting the above quote and ending with:

"I drink your milkshake! I drink it up!"
…before bludgeoning the man to death with a bowling pin.

Much like Daniel Plainview, the U.S. has amassed a vast amount of wealth and delivered decades of prosperity to its citizens since the dollar ascended to reserve currency status after World War II. For years, we have drunk the world's milkshake—drawing in global liquidity to finance our growth and lifestyle.

We have never in the history of this great nation tried to reverse-engineer decades of structural excess this quickly. In attempting to fix both the trade and budget deficits simultaneously through aggressive tariffs and sweeping government reforms risks destabilizing markets and undermining the dollar's global standing. We risk not only breaking the straw and shattering the glass, leaving no one able to drink the milkshake, but bludgeoning the American consumer in the process. A consumer who for decades has savored the sweet taste of global "milkshake" liquidity.

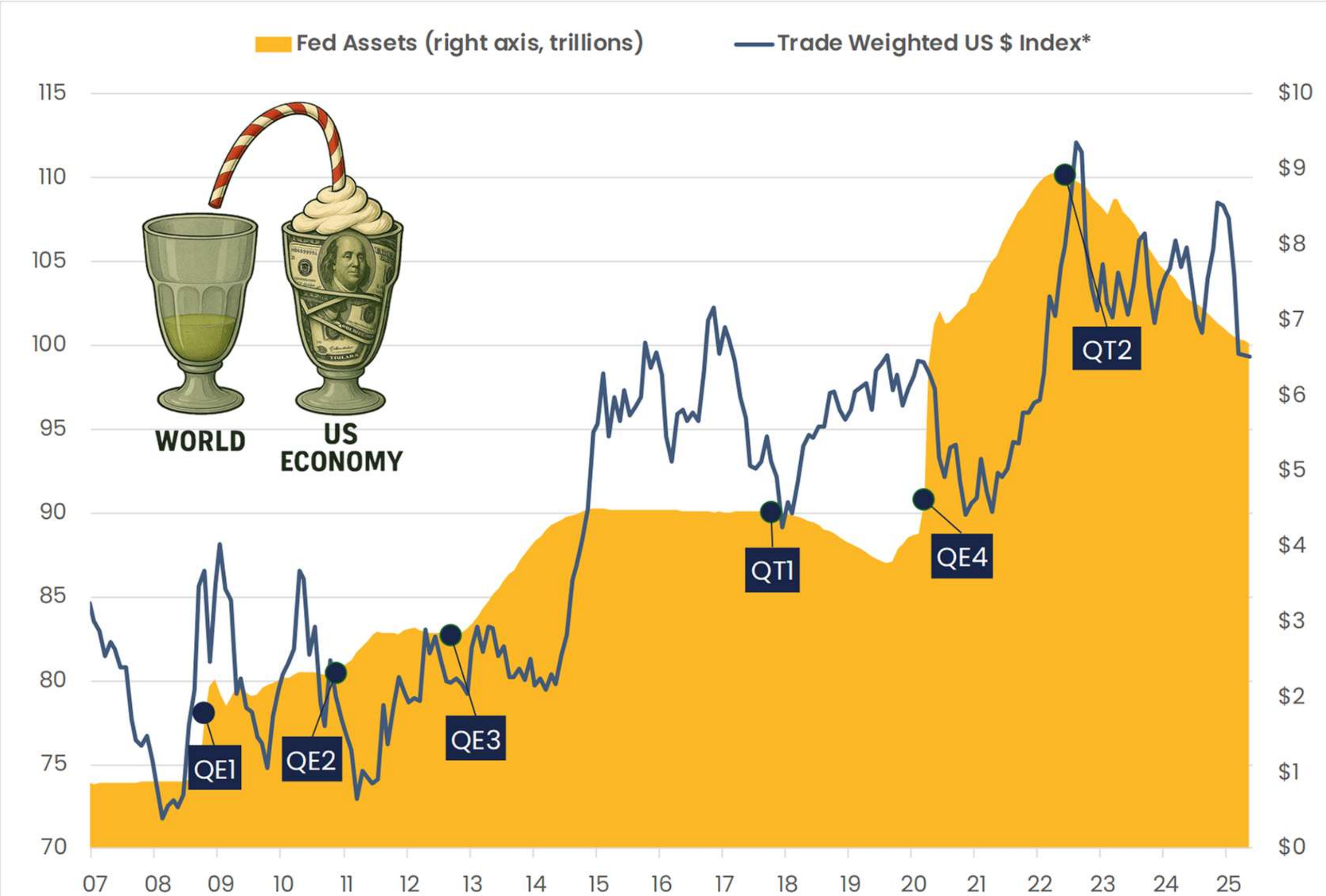
We cannot hedge policy direction nor predict every move, but we can observe and prepare for volatility. Recognizing the shifting flows of liquidity and narratives is essential to navigating what lies ahead. This understanding will be critical to capturing emerging trends, enhancing our behavioral and fundamental approach to stock selection.

With this in mind, we present several compelling charts that form part of a larger mosaic.

The following figures explore topics including:

- **The Trade-Weighted Dollar vs. Fed Balance Sheet Expansion**
- **Fiscal & Trade Policy Uncertainty Indices Since 1980**
- **Total U.S. Debt and Deficits as % of GDP (1900–2025)**
- **Interest Expense and Debt Maturity Wall**
- **Corporate Profits Since 1945 and Trade Flows Since 1900**
- **Composition of U.S. Debt Holders and Foreign Holdings of U.S. Treasuries**
- **Central Bank Gold Purchases**

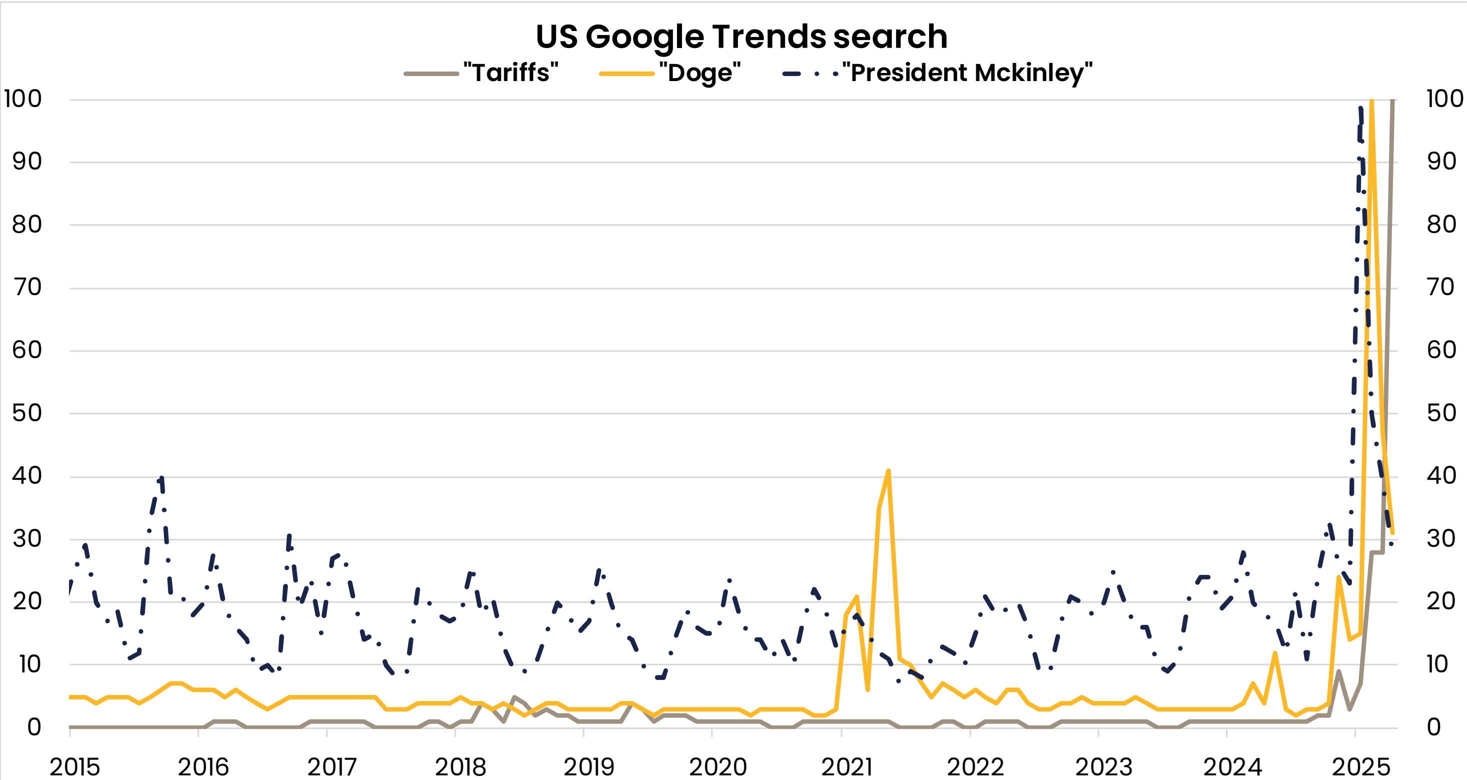
Figure 1: The Dollar Milkshake Theory—The U.S. $ has appreciated by 50% between QE1 to QT2



Source: Investing.com, Center for Financial Stability, Board of Governors of the Federal Reserve System (US)

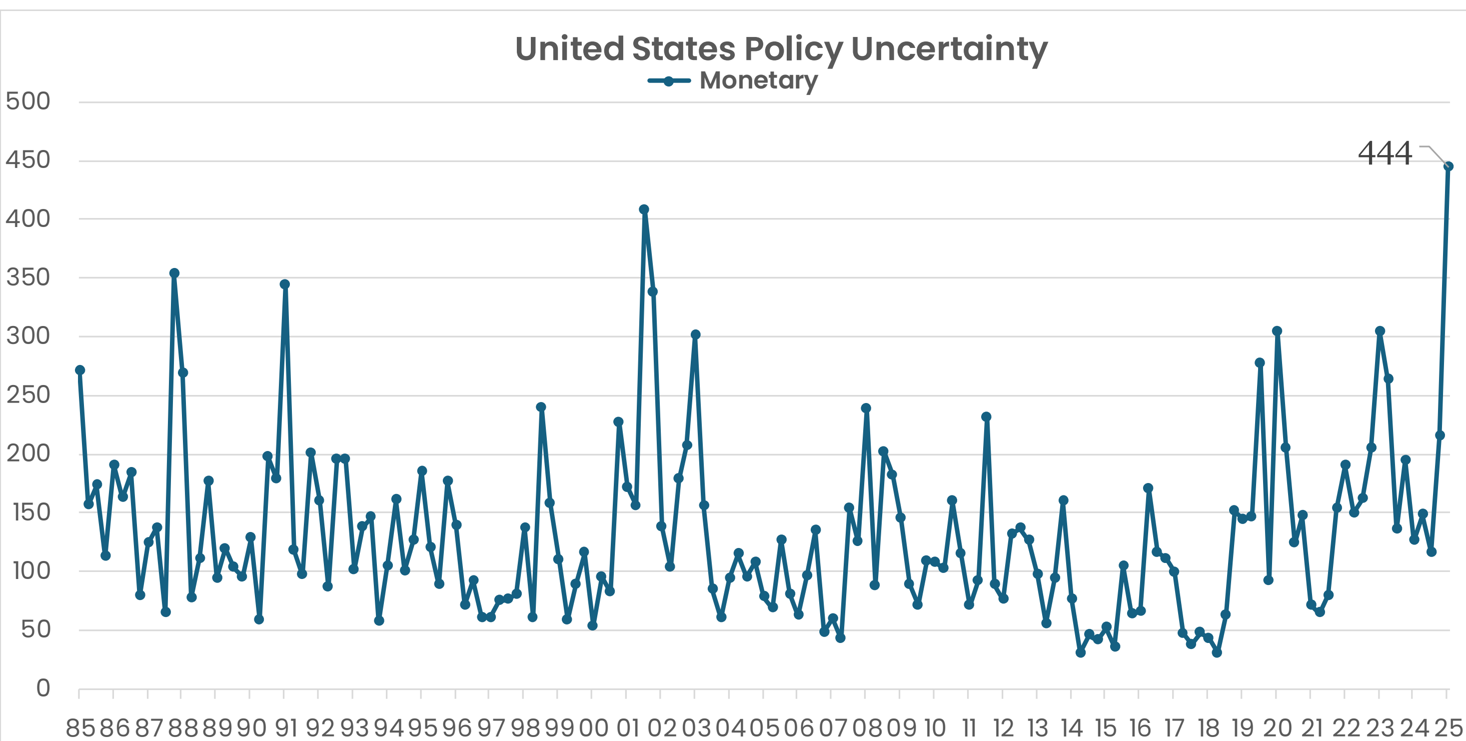
*A measure of the value of the U.S. dollar relative to the currencies of its major trading partners, weighted by the volume of trade with each country.

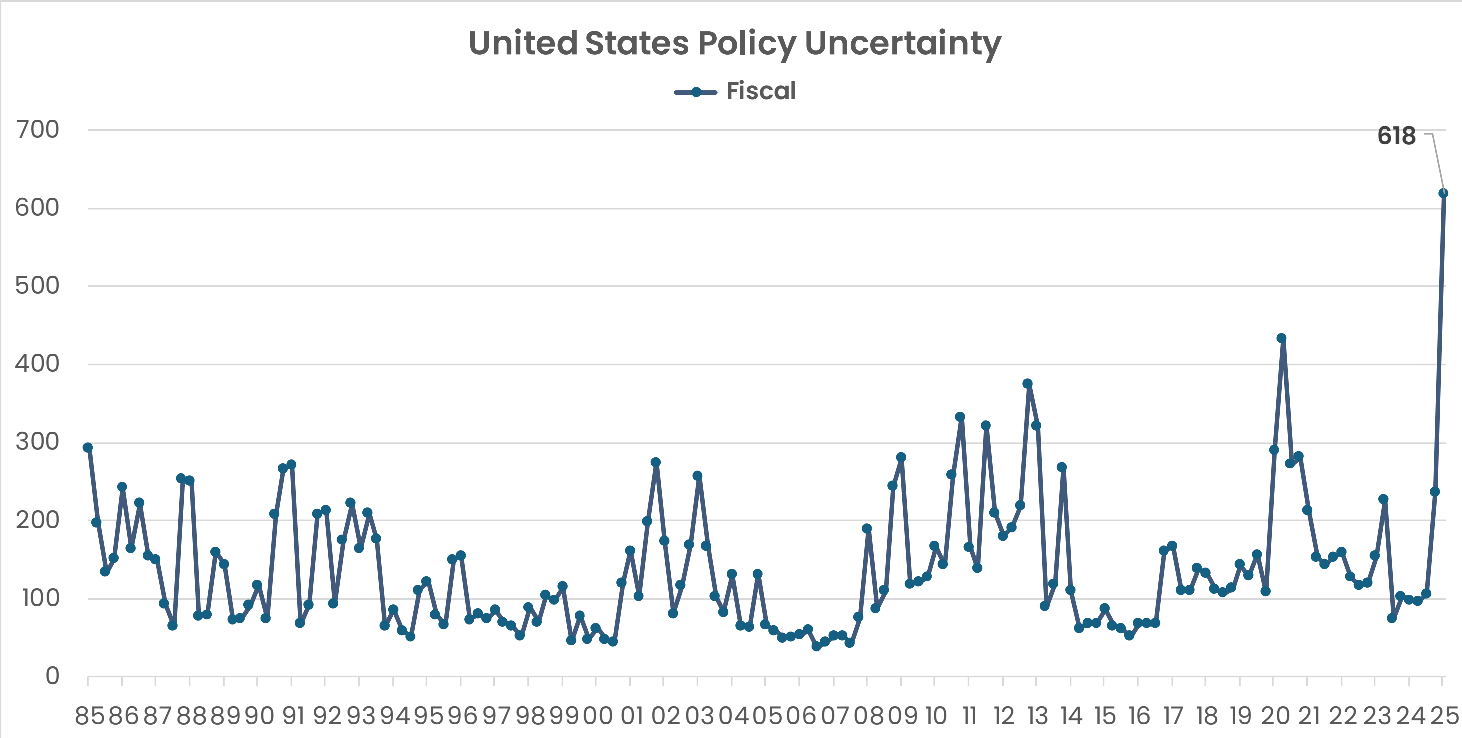
Figure 2: Google search interest in "tariffs" and "doge" spiked during the 1H25

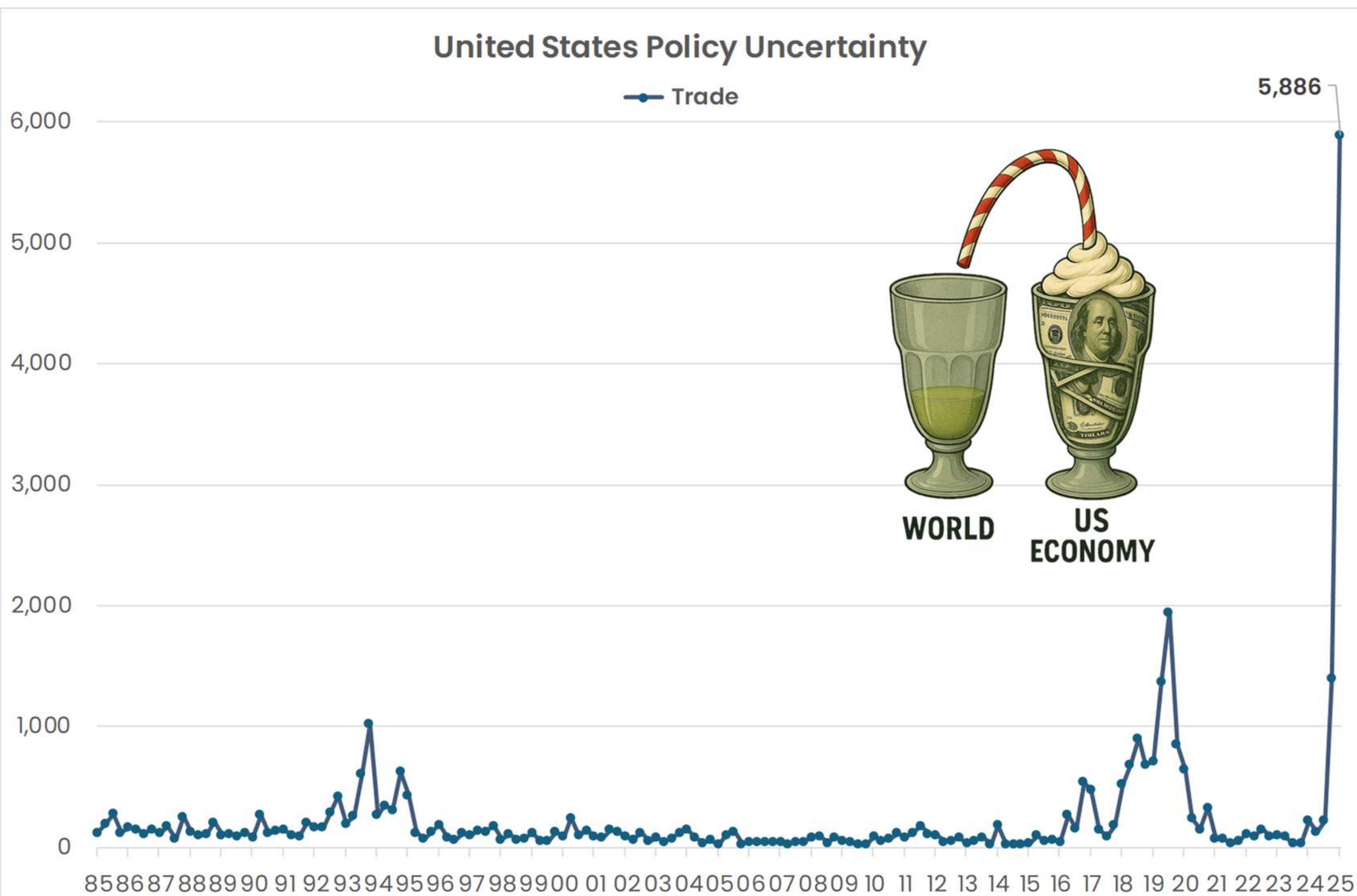


Source: Google Trends

Figure 3a,3b & 3c (next three charts): Policy uncertainty hits generational highs across Monetary, Fiscal, and Trade arenas

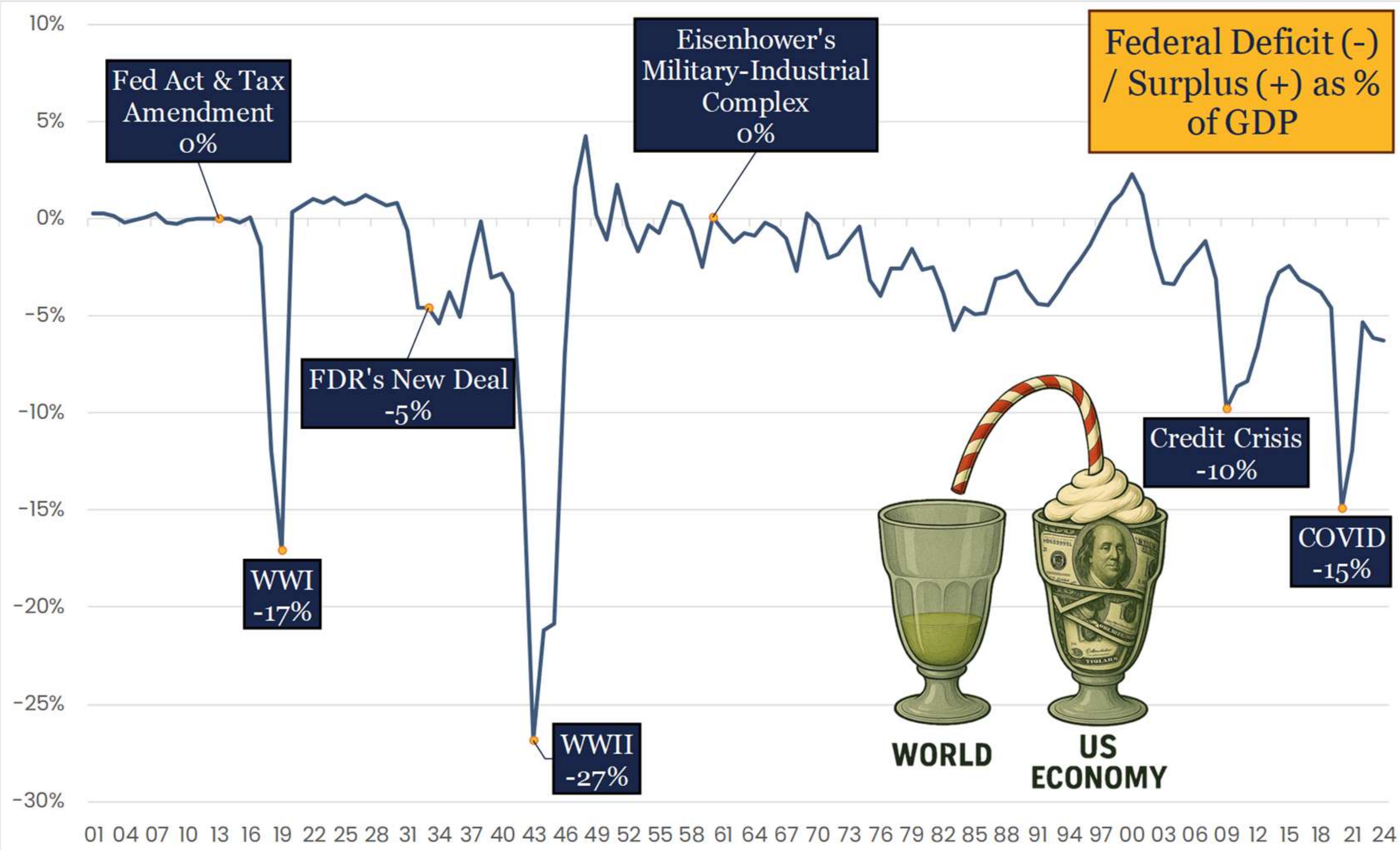






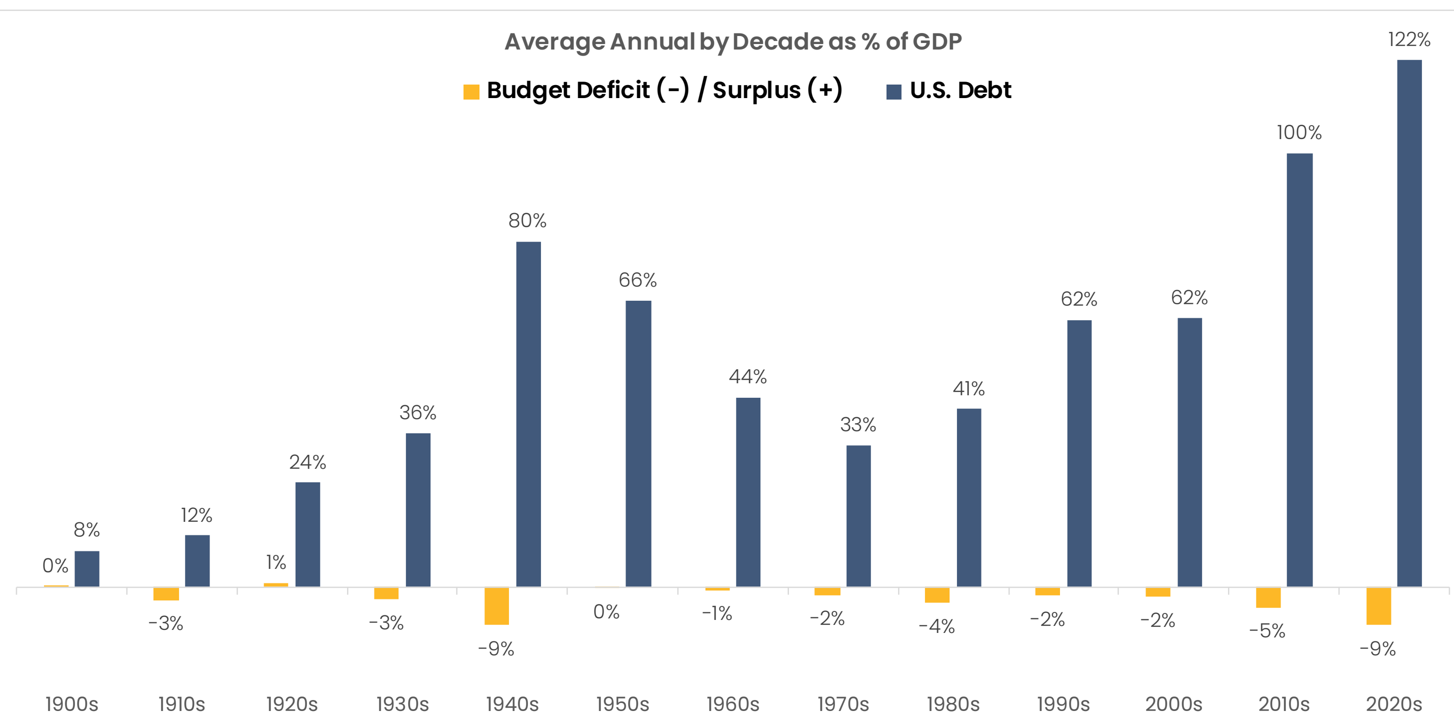
Source: Policyuncertainty.com

Figure 4a: A century of U.S. budget deficits and surpluses since 1900



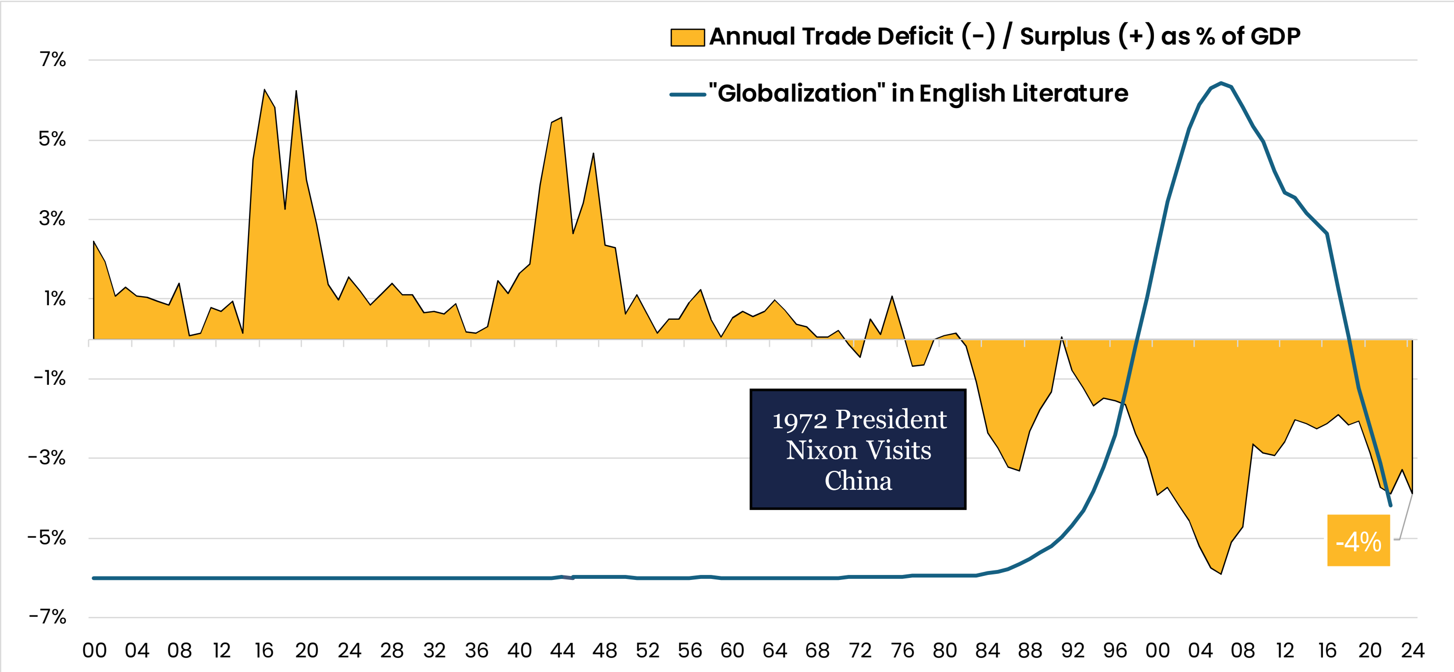
Source: U.S. Bureau of Economic Analysis, U.S. Office of Management and Budget

Figure 4b: U.S. debt at unprecedented levels, driven by structural deficits rivaling the 1940s



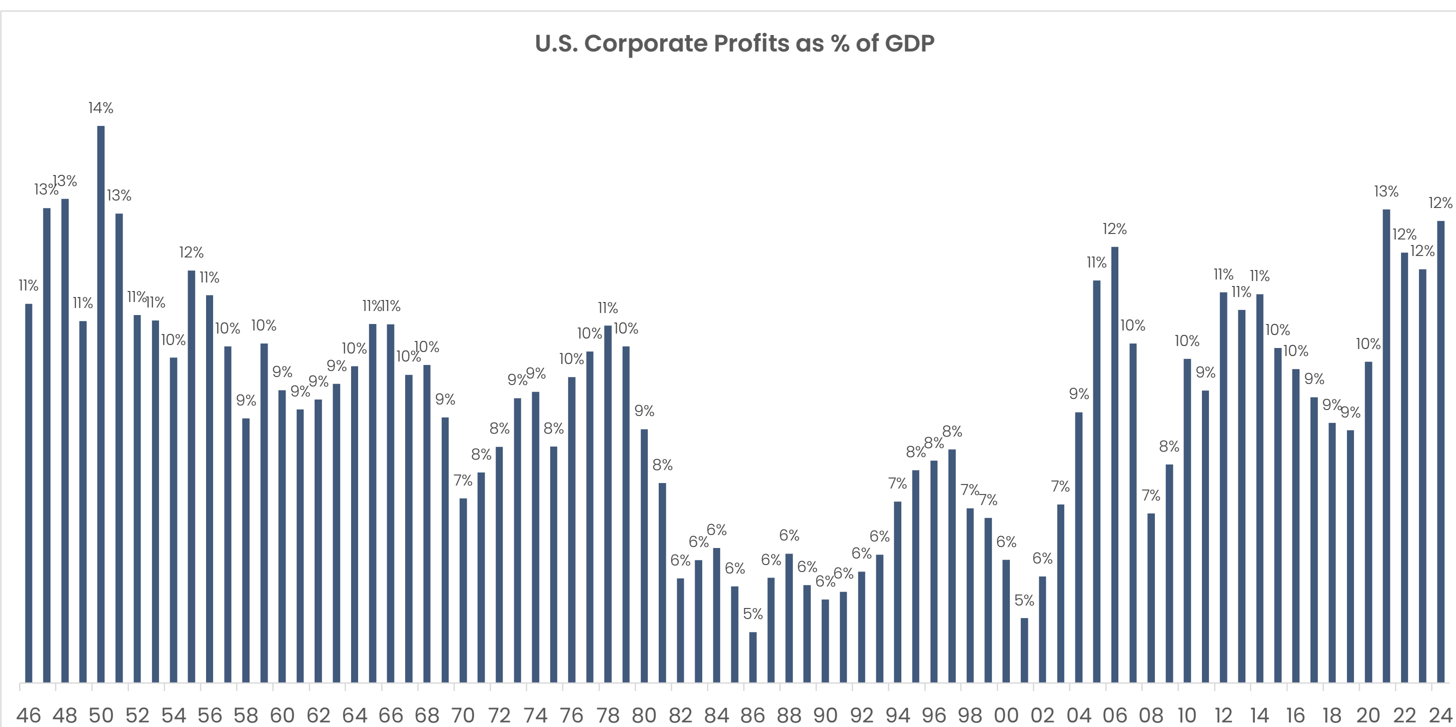
Source: FiscalData at Treasury.gov, U.S. Bureau of Economic Analysis, U.S. Office of Management and Budget

Figure 5: The Globalization Inflection Point — U.S. Trade Balance before and after Nixon's China visit



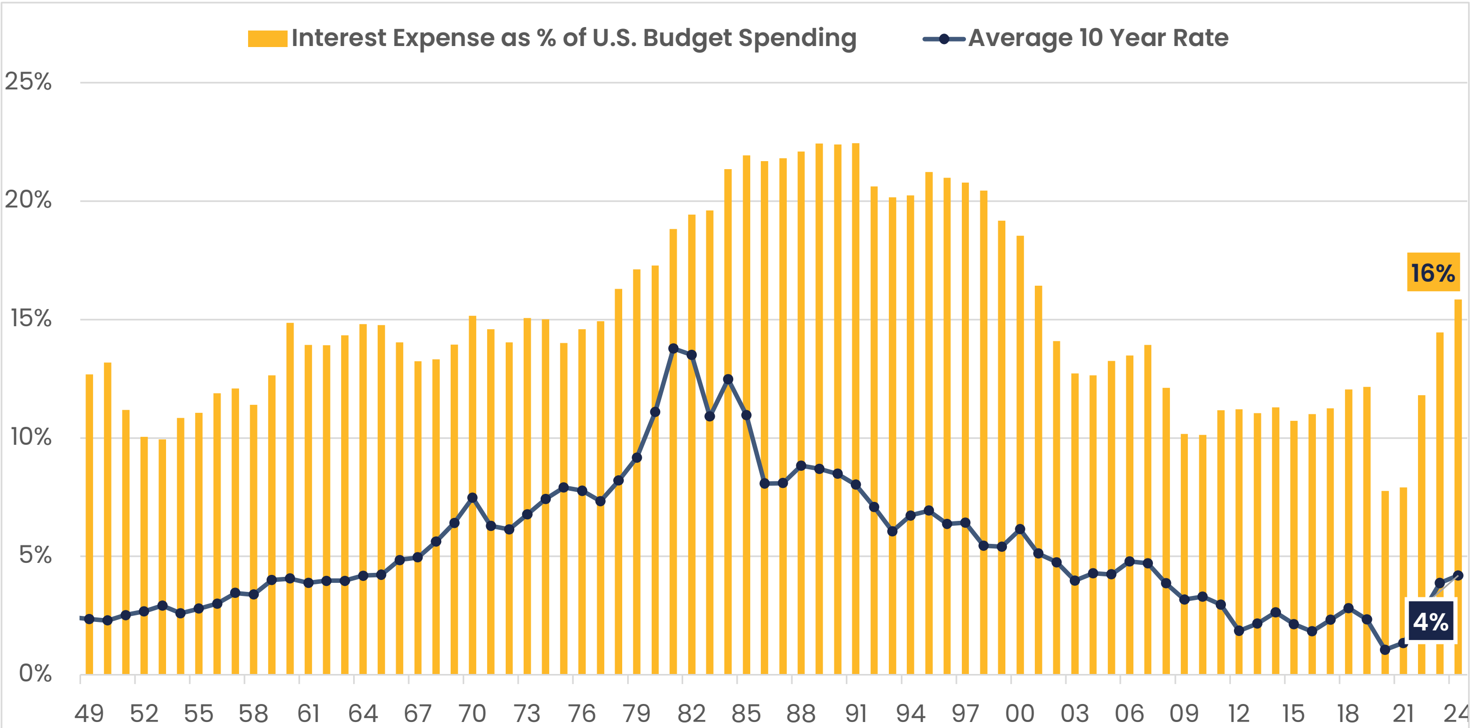
Source: U.S. Bureau of Economic Analysis, United States Census Bureau, & Googles nGram

Figure 6: Corporate profits surged to all-time highs, fueled by globalization



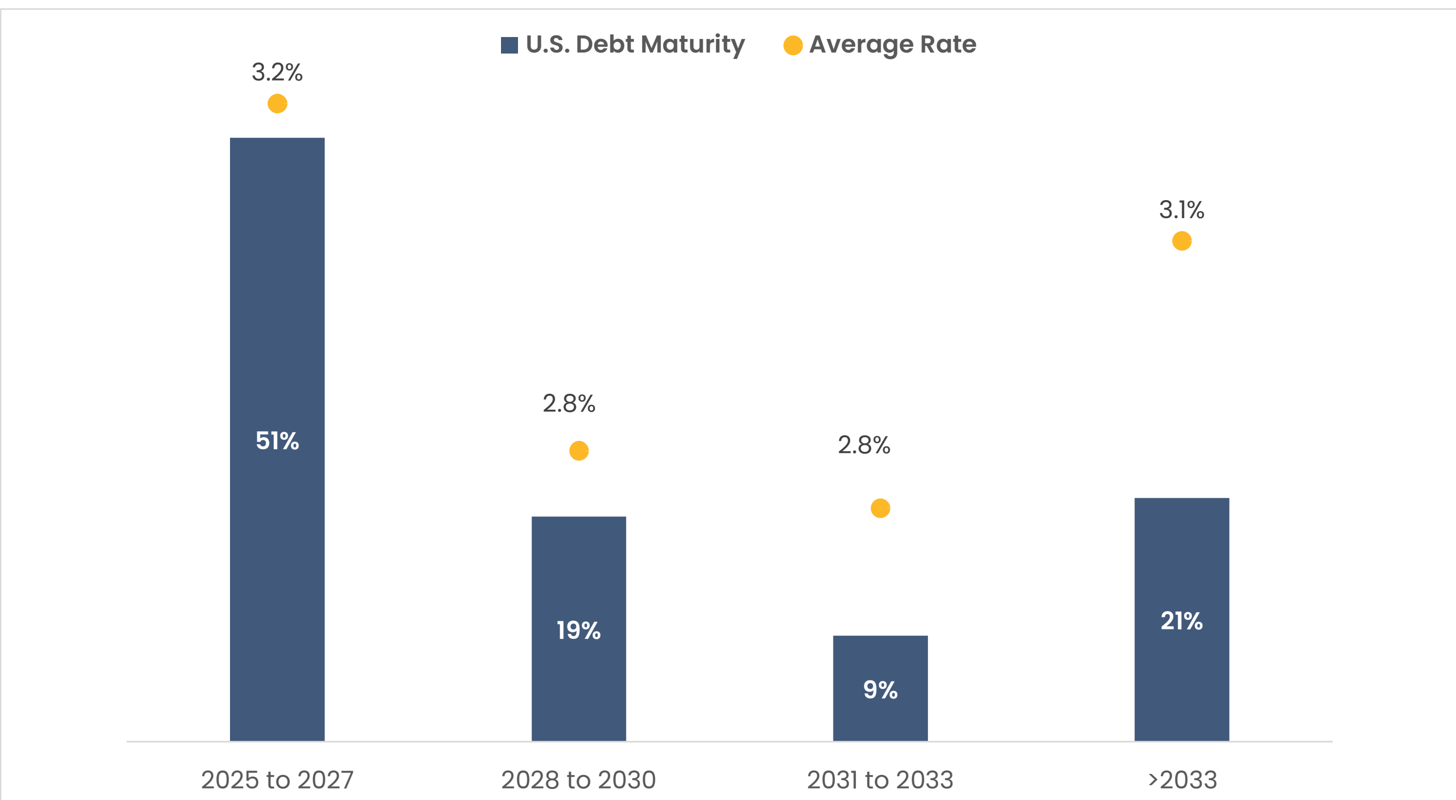
Source: U.S. Bureau of Economic Analysis

Figure 7a: Interest expense is the second largest line item in the federal budget behind social security



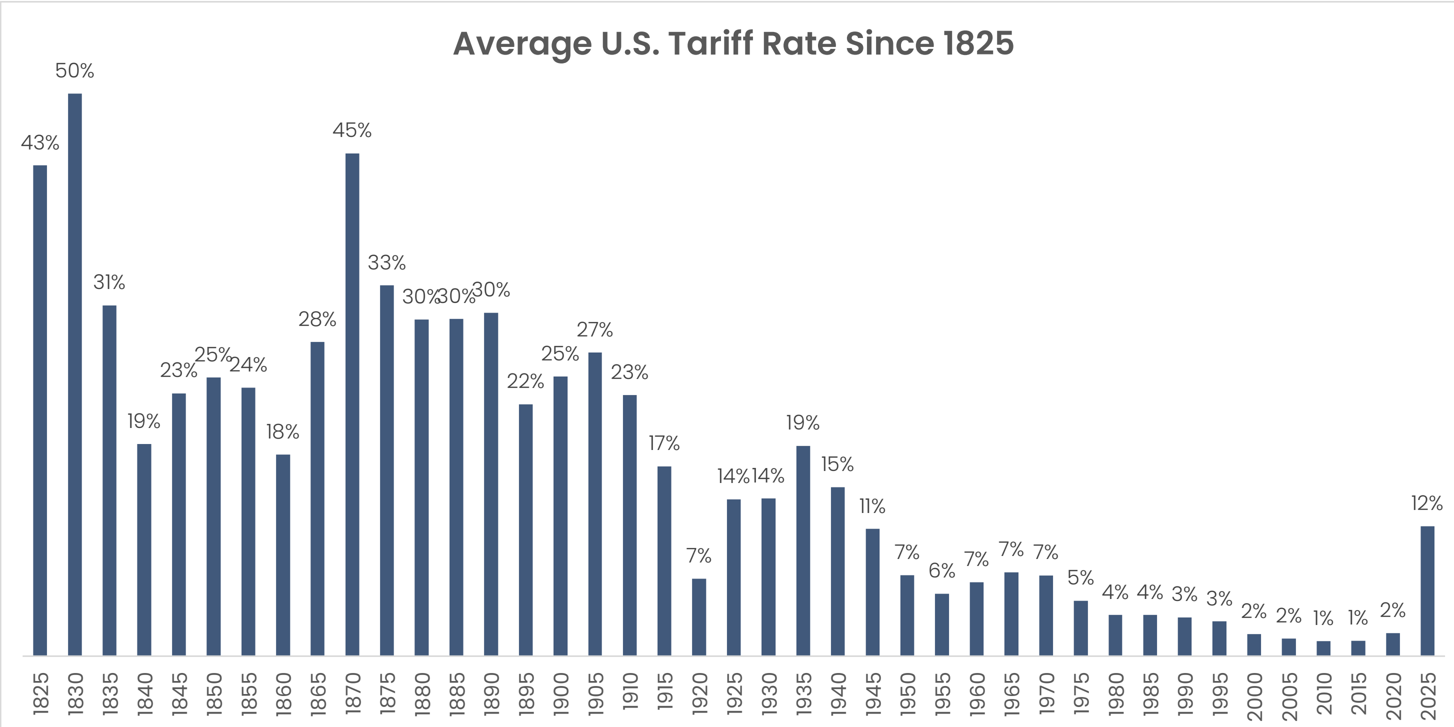
Source: Fiscal Data at treasury.gov, U.S. Bureau of Economic Analysis

Figure 7b: The Coming Wave—U.S. debt faces major refinancing overhang



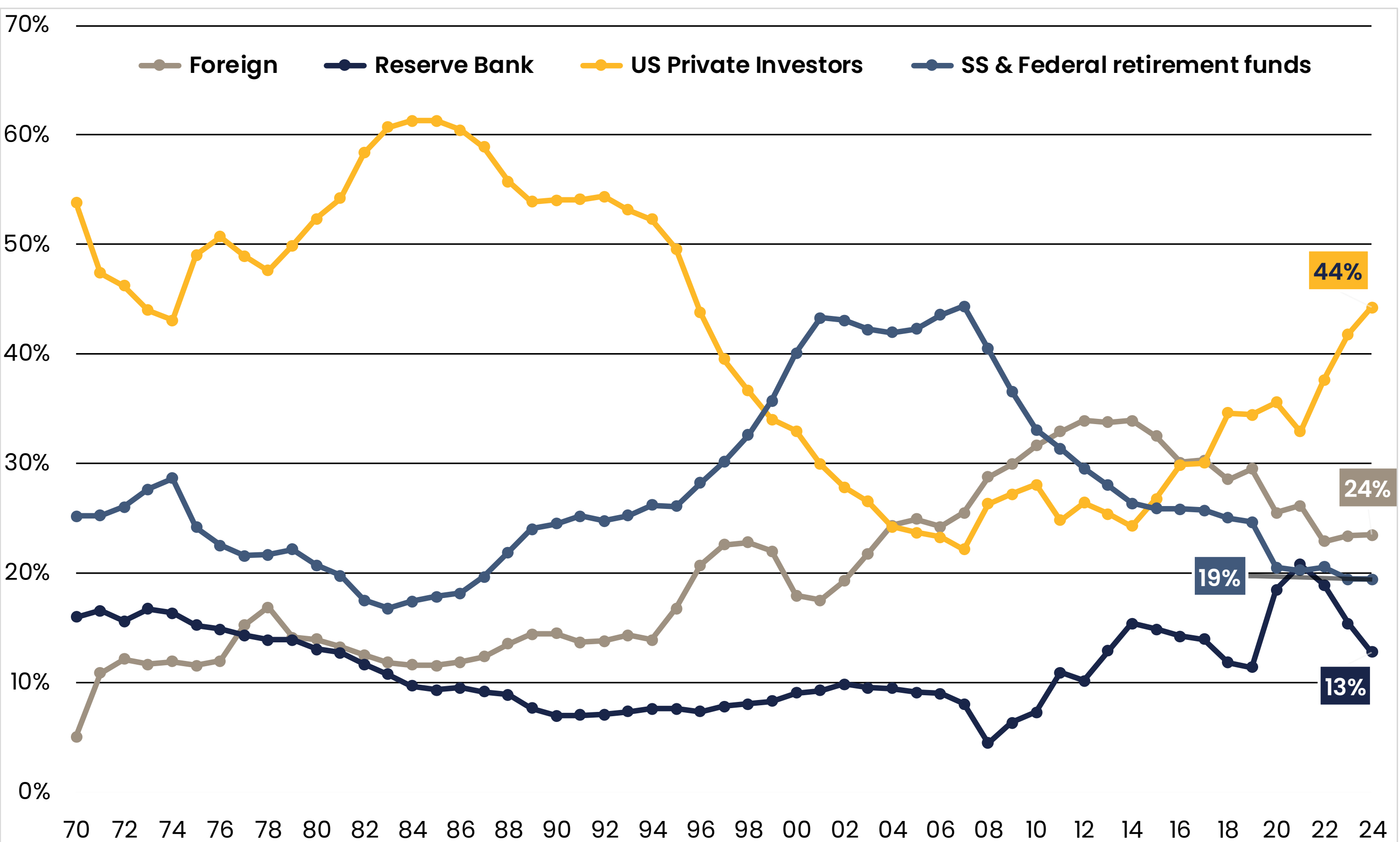
Source: Fiscal Data at treasury.gov

Figure 8: If Trump's tariffs stick, it will signal a massive shift in global relations — one not seen since the 1940s.



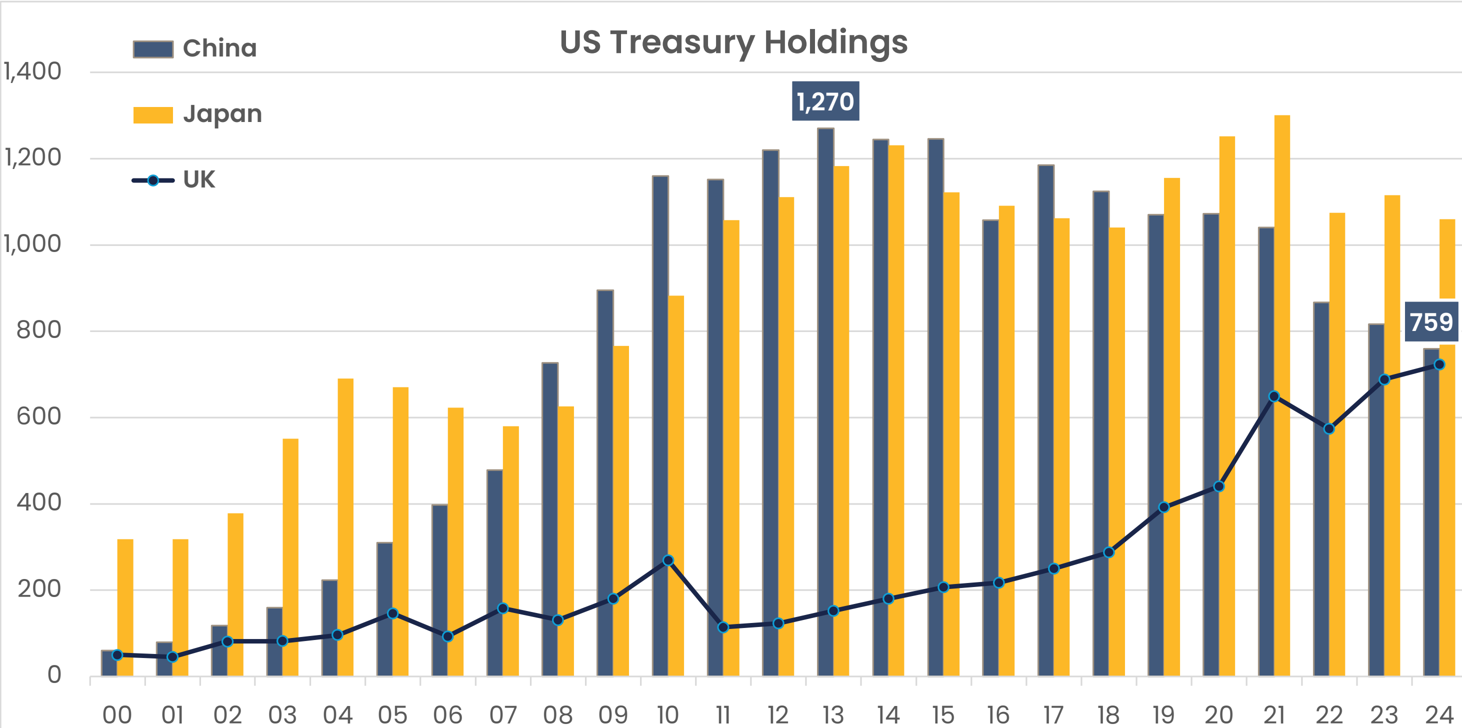
Source: Tax Foundation

Figure 9: U.S. private investors now hold 44% of outstanding Federal Debt—more than double their share two decades ago



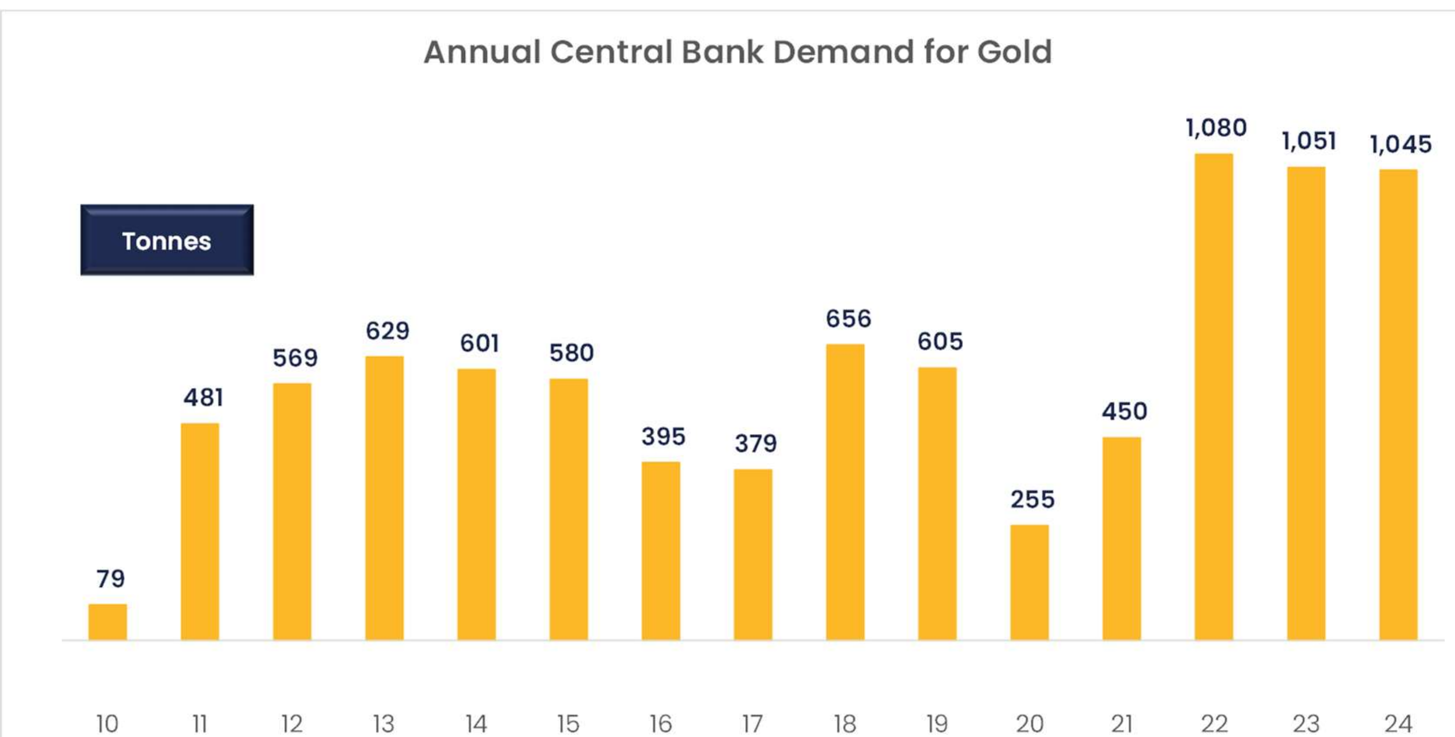
Source: U.S. Department of the Treasury

Figure 10: China has sold nearly half of their U.S. debt holdings since Trump 1.0



Source: U.S. Department of the Treasury

Figure 11: While Central Banks are accumulating more bullion



Source: World Gold Council

About CS McKee

Since 1931, CS McKee has been helping institutional investors navigate financial markets with a steady hand, disciplined strategies, and an unwavering commitment to their success. While our investment approach is rooted in time-tested principles, we're always evolving — balancing consistency with fresh insights to adapt to an ever-changing financial landscape.

What does it look like in practice?

We take a disciplined, research-driven approach to managing assets, staying true to our proven philosophy and process while embracing innovation where it adds value. At the end of the day, it's all about our clients and helping them achieve their financial goals with the personalized service, dependability, and partnership they've come to expect from us.

Proudly Serving a Wide Breadth of Institutional Clients

Our hallmarks of exceptional client service and time-tested investment strategies have earned the trust of a diverse roster of institutional clients. While we got our start in Pennsylvania, our clientele now spans across the country, reflecting our national reach and reputation.

Disclosures:

CS McKee is an investment adviser registered under the Investment Advisers Act of 1940. Registration as an investment adviser does not imply any level of skill or training. For more information, please visit: https://adviserinfo.sec.gov/ and search for our firm name. The information presented in the material is general in nature and is not designed to address your investment objectives, financial situation or particular needs. Prior to making any investment decision, you should assess, or seek advice from a professional regarding whether any particular transaction is relevant or appropriate to your individual circumstances. Although taken from reliable sources, CS McKee cannot guarantee the accuracy of the information received from third parties.

The opinions expressed herein are those of CS McKee and may not actually come to pass. This information is current as of the date of this presentation and is subject to change at any time, based on market and other conditions. Index performance used throughout this presentation is intended to illustrate historical market trends and performance. Indexes are unmanaged and do not incur investment management fees. An investor is unable to invest in an index. The performance shown is not a reflection of Foundry Partner's Portfolios. Past performance is not indicative of future results.

Charts, diagrams and graphs, by themselves, cannot be used to make investment decisions. This information does not constitute a solicitation nor an offer to buy or sell any securities.

About The Authors

Mario Tufano, CFA
Senior Portfolio Manager,
Small Cap Equities

Mario Tufano is a Senior Portfolio Manager of Small Cap Equities for CS McKee, following its acquisition of Foundry Partners. Mario started in the industry in 2002 and had been with Foundry Partners since the company's transaction with Dreman Value Management (DVM) in June of 2016. He joined DVM in 2007 as a Senior Securities Analyst and was promoted to Associate Portfolio Manager in 2010. He is responsible for research of new investment ideas as well as current portfolio holdings for the firm's Small and Mid Cap Value products. Prior to joining the firm, he was an Associate Director and Equity Analyst at UBS Investment Bank covering the Consumer Staples and Discretionary sectors.

Mr. Tufano graduated from Pennsylvania State University with a B.S. in Finance. He is a CFA charterholder and is a member of the New York Society of Security Analysts (NYSSA).

Mark Roach
Director,
Small & Micro Cap Equities

Mark Roach is a Director of Small and Micro Cap Equities at CS McKee, following its acquisition of Foundry Partners. Mark started in the industry in 1995 and had been with Foundry Partners since the company's transaction with Dreman Value Management (DVM) in June of 2016. He was with DVM from late 2006-June 20, 2016 in a similar capacity. Prior to joining DVM, Mr. Roach was a Portfolio Manager at Vaughan Nelson Investment Management, managing a small cap product from 2002 through 2006. Mr. Roach has significant experience in working with institutions, pensions and endowments and is well known in the consulting and high net worth community. Mr. Roach served as a security analyst from 1994 to 2001 for various institutions including Fifth Third Bank, Lynch, Jones & Ryan and USAA.

Mr. Roach graduated from Baldwin Wallace College with a B.A. in Business, and earned a MBA from the University of Chicago's Booth School of Business. In addition, Mr. Roach is a former board member on the Rice University Wright Fund.

Contact Information:

Jason Thon:
Director, Marketing
& Communications
jthon@csmckee.com

Chris Luke:
Chief Marketing Officer
cluke@csmckee.com

csmckee.com
information@csmckee.com
412.566.1234