Fisher Investments™ Institutional Group

MARKET PERSPECTIVES
REVIEW & OUTLOOK

SECOND QUARTER
2025

SECOND QUARTER 2025 REVIEW & OUTLOOK

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SECOND QUARTER 2025 REVIEW & OUTLOOK
EXECUTIVE SUMMARY

July 14, 2025

PORTFOLIO THEMES

- We believe the global bull market will continue, despite fears around recent volatility, fiscal policy and geopolitics.
- We expect European equities and Value to continue to lead global performance in the second half of 2025, building on their initial start in H1, albeit with expectations for US and Growth to also fare well.
- Easing global inflation has led to many central banks cutting rates, resulting in a steeper yield curve and acting as a tailwind to non-US countries as the Fed mulls over their own course.

MARKET OUTLOOK

- **Tariffs Not Playing Out as Feared:** With pending court challenges, new trade deals with countries, and underwhelming tariff collections, US tariff impact has been better-than-feared. Worst-case scenarios were priced in in April but as they failed to come to fruition markets bounced back sharply.
- **Post-Correction Gains Do Not Signal the End:** Retracing pullbacks tend to trigger selloff behavior from investors, but enduring volatility often lays the groundwork for renewed upside and further gains.
- **Reset Sentiment Should Provide Bull Market Fuel:** Fresh skepticism inside and outside the US from tariff and political developments lower the bar of expectations, setting the stage for positive surprise and a continuing bull market.

Global equities proved a timeless truth about corrections in Q2, rebounding sharply from "Liberation Day"'s steep fall to finish June at new all-time highs. While the correction started in mid-February, the bulk of its drop and full recovery lived in Q2, including the two-day, -8.6% slide after April 2's tariff shock.[i] Yet the round trip netted out to an 11.5% MSCI ACWI Index quarterly rise, reminding the world how quickly markets move on after pricing in even real negatives.[ii] Despite being the initiator of the "Liberation Day" volatility, the US fared well, ending the quarter up 10.9%.[iii] Emerging Markets followed in step and edged out other major indices, returning 12.0% in Q2.[iv]

Equities' downswing was an archetypal correction, classic in every way. It was a short, sharp shock, featuring a huge scary story: tariffs. As Q1's Review discussed, we don't think tariffs are good policy, hitting the imposer harder than the targets. But markets overshot, pricing worst-case scenario estimates rapidly. This reset sentiment, positioning equities for a big relief rally when things didn't go as badly as feared. Markets rose as President Donald Trump delayed reciprocal tariffs and negotiated trade deals, while lower-than-expected tariff revenues eased fears of the economic effects. Even the ongoing conflict in the Middle East has hardly disrupted markets' fast recovery.

i Source: FactSet, as of 07/08/2025. MSCI ACWI Index return with net dividends, 04/02/2025 – 04/04/2025, in USD.

ii Ibid. MSCI ACWI Index return with net dividends, 03/31/2025 – 06/30/2025, in USD.

iii FactSet, as of 07/08/2025. S&P 500 Index returns, 03/31/2025 – 06/30/2025, in USD.

iv FactSet, as of 07/08/2025. MSCI EM Index returns with net dividends, 03/31/2025 – 06/30/2025, in USD.

April's tariff rollercoaster drove sharp volatility in EM as confusion reigned early in the month and uncertainly lingered thereafter. However, on April 9, Trump paused all reciprocal tariffs for 90 days except on China, citing many nations' efforts to strike deals. US-China trade tensions appeared to ease further in June, after the countries signed a deal on June 25 to relax export restrictions with each other. Although bilateral tariffs remain higher than they were at 2025's start, the agreement suggests fear of worst-case trade scenarios will likely prove excessive, lifting sentiment. EM equities should also benefit from recent US dollar headwinds fading and continue to follow the trend of outperformance with Republican US presidents.

In our view, Q2's rally is a preview of strong full-year returns. We remain bullish, and our forecast remains from the beginning of the year, Europe and Value leading with the US doing just fine. Equities have already exceeded many professional investors' consensus forecasts. Sentiment, particularly after the correction reset it lower, remains dour overseas and weakened in the US, creating ample room for the global economy and earnings to beat expectations. Europe and value equities are leading[v], though US and growth equities are doing fine. Politics remains as divisive as ever, yet political uncertainty abates as policies and possibilities become clearer, like them or not. Subdued global money supply growth points to benign inflation. Yes, investors have valid concerns, but all are discussed too widely to have much effect on equities, in our opinion.

Bond markets' behavior was also emblematic of a correction, especially in corporate bonds, where yield premiums over Treasuries widened substantially amid equity market volatility, then reverted to historically low levels, a reminder that bonds aren't immune to short-term sentiment swings. As with equities, there was a fearful headline accompanying long-term interest rates' volatility: debt and deficit fears tied to the "One Big Beautiful Bill Act" (OBBBA) and fiscal policy debates in the UK, France, Japan and elsewhere. Slight demand wiggles at May bond auctions caused outsized reaction. The frenzy died down as rates eased and subsequent auctions undercut the fear. The volatility netted out to a basically flat quarter for 10-year US Treasury yields, in line with our forecast for rates to stay relatively rangebound.

The OBBBA remains top of mind for many, but we don't see surprise power here for equity or bond markets. The debate was too noisy and public, the associated forecasts heavily scrutinized. The same goes for debt fears across Europe and Japan, which hide an improving economic landscape. Political uncertainty is easing in America, as markets reacclimate to this presidential administration's style. It should continue falling further as budget debates wind down overseas.

Meanwhile, to no fanfare, the global yield curve has steepened—especially outside the US, further supporting portfolio positioning. Easing inflation pressures have enabled central banks to cut rates, and consensus expectations are for this to continue. The US would likely benefit from rate cuts and a steeper yield curve as well, but so far the Fed lags behind other regions. The more Trump pressures the Fed to cut rates, the more it incentivizes Fed head Jerome Powell to wait. His primary job at this juncture is to protect what passes for Fed "independence." This isn't to say the Fed won't eventually cut, but Powell has had incentive to wait and may continue. Hence, steeper yield curves are likely more of a tailwind outside the US, supporting our value-heavy European positioning in global strategies.

v FactSet, as of 07/08/2025. MSCI EAFE Index returns with net dividends, 12/31/2024 – 06/30/2025, in USD.

While it is rare for equities to suffer more than one correction in a year, further volatility is always possible. Lingering tariff uncertainty is a wildcard. The August 1 expiration of Trump's reciprocal tariff pause for some countries is one source of such uncertainty. But there are others, including the status of deals and pending appellate court reviews of challenges to Trump's main tariffs, to name a few.

Regardless of short-term wiggles, we think this bull market has significant room to run. Breaking even following a correction creates selloff pressure but is part of the way sentiment normally resets after a correction. We believe these headline fears are part of the wall of worry this bull market should continue to climb. New highs after a correction tend to breed new highs, not fresh declines, and is the reward for discipline through endured volatility.

GLOBAL UPDATE AND MARKET OUTLOOK

August 6, 2025

MARKET RECAP

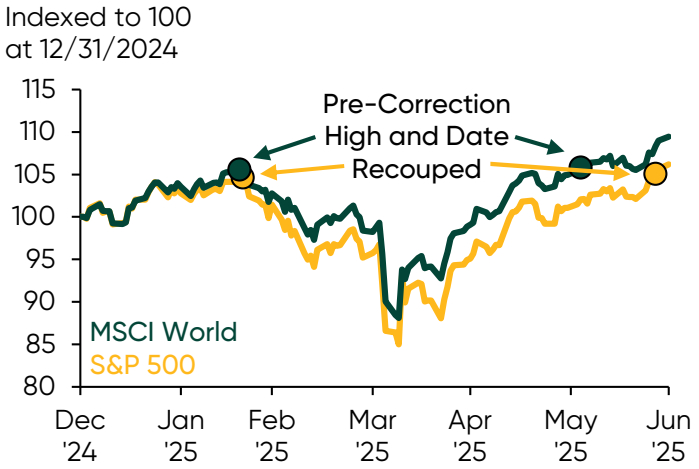
THE CORRECTION AND BEYOND

Amid the depths of the first half's correction in April, few could envision 2025 turning out to be a good year. Blinded by volatility, most could only see more downside ahead in what they were sure was a bear market driven by tariffs.

But we remained bullish. For one, we laid out several scenarios in our Q1 Review, noting the greatest likelihood was tariffs' effects being far smaller than the worst-case scenario markets had pre-priced. We warned of the risks of trying to time widely-watched, near-term volatility and counseled patience. The fast rebound that followed illustrates that logic's huge importance.

The correction started in February, but much of the decline—and the full recovery—lived in Q2. That recovery came unannounced, despite widespread and morphing fears, chiefly tariffs and their mooted downstream effects. Markets pre-priced worst-case scenario fears into global equity prices. Once they did, an accelerated rebound followed, with world equities roundtripping to new all-time highs by June 3 and US equities getting there June 26.

EXHIBIT 1: THE FIRST HALF'S CORRECTION AND RECOVERY



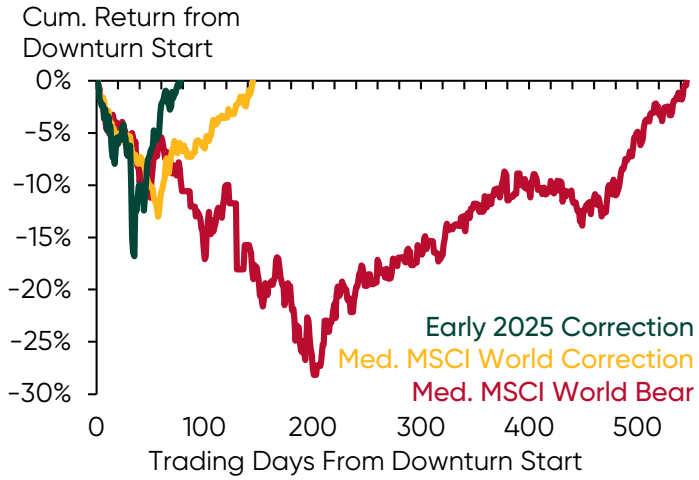
Source: FactSet, as of 07/07/2025. S&P 500 Total Return and MSCI World Index with net dividends, 12/31/2024 – 06/30/2025.

Many doubt the quick recovery, labelling it as "too far, too fast," a normal post-correction sentiment feeding behavioral investment errors like breakevenitis. But these likely create more problems than they solve. Besides, there is nothing atypical about last quarter's swift slide and rapid recovery. Exhibit 2 demonstrates this, showing Q2s downturn and recovery closely resemble the median correction and recovery (see next page).

Some see a correction as a sign of a shaky bull market, but we think this is backward. Corrections' sting and lingering fear helps reset expectations lower. This takes potential ebullience off a bull market, helping facilitate the positive surprise that fuels rising equities. A strong bull market *needs* some skepticism or pessimism. Corrections help foster it. This is why history's longest bull market, in 2009 – 2020, featured eight.[vi]

vi Source: FactSet, as of 07/07/2025. Count based on MSCI World corrections, 03/09/2009 – 02/12/2020.

EXHIBIT 2: THE CORRECTION'S RAPID REBOUND



Source: FactSet, as of 07/11/2025. MSCI World Price Index, 02/18/2025 – 06/06/2025 and median corrections and bear markets, 12/31/1975 – 12/31/2024.

From here, our bullish forecast remains intact. Already, many non-US markets have topped too-dour consensus forecasts entering 2025—and appear en route to far greater returns than virtually any professional forecaster expected. Even the S&P 500, lagging most major nations and up 6.2% at 2025's midpoint, tracks the 12.2% median professional forecast documented in our Q4 2024 Client Review & Outlook, *despite* the correction.[vii] Few thought this possible just three months ago, with many pundits slashing forecasts following the steep correction.

FORECAST RECAP

Even beyond broad market movement, much of this year is playing out as we expected.

Equities outside America, especially Europe, lead. In January, we noted sentiment was too dour toward equities outside the US. This helped deliver marked non-US and European leadership. However, tariffs also play a role.

While many see tariffs as policy that protects, encourages or fosters domestic industry over imports, this isn't true. Tariffs hit the *imposing* nation harder than targeted countries. They can sway prices, interfere with businesses' plans and discourage investment. Many US industries prove the point, including steel. Long protected by a complicated web of tariffs, import quotas and more dating to the 1960s, the industry still sagged. The reason? Tariffs and protectionism discouraged investment in modernizing mills—because the future of those policies was by nature uncertain.

As we detailed last quarter, Trump's tariffs stoke uncertainty. To see this, look to markets, the ultimate truth-tellers. Despite the raft of allegedly "America First" policies, US markets have plunged from near the top of the world's performers last year to near the bottom in 2025's first half. Exhibit 3 shows you this, using the MSCI All-Country World Index's 47 constituent nations. America ranks number 37—and it took a strong June rally to get even there (see next page).

The countries leading in 2025's first half include some telling examples. Threats toward Canada and Mexico had many thinking these two were particularly vulnerable to Trump's tariffs. Yet the MSCI Canada's 15.5% first-half return more than doubles the MSCI USA's 6.3%.[viii] And what of Mexico? It rose 30.9% in the first half.[ix] Even China—the major target of tariffs—rose 17.3%, easily eclipsing US equities.[x] We expect this non-US leadership to persist, fueled by tariffs' effects, dour sentiment toward non-US equities and the steepening global yield curve—a fundamental positive for the value firms that dominate Europe.

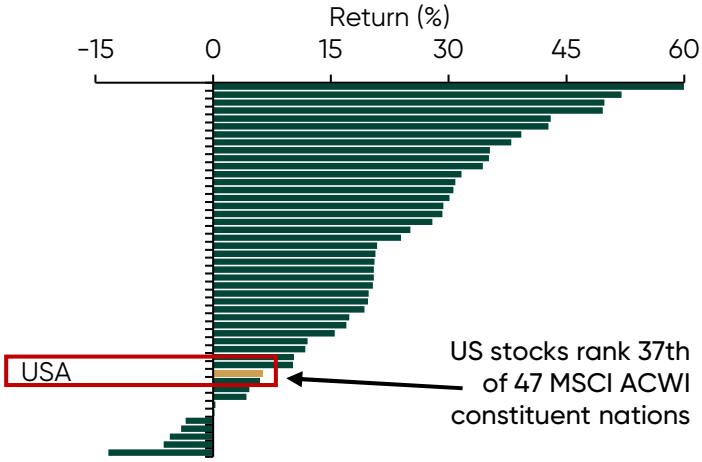
vii Source: FactSet, as of 07/08/2025. S&P 500 total return, 12/31/2024 – 06/30/2025.

viii Source: FactSet, as of 07/16/2025. MSCI Canada return with net dividends and MSCI USA return with gross dividends, 12/31/2024 – 06/30/2025.

ix Ibid. MSCI Mexico return with net dividends, 12/31/2024 – 06/30/2025.

x Ibid. MSCI China return with net dividends, 12/31/2024 – 06/30/2025.

EXHIBIT 3: FIRST HALF RETURNS BY COUNTRY



Source: FactSet, as of 07/16/2025.

Value outperformed alongside Europe and non-US equities. To those who understand the overlap between style and geography, this wouldn't shock. But many pundits overlook the fact America is growth-heavy while value dominates Europe. Part of this year's non-US leadership is about expectations' being too high in America entering 2025. But expectations were also notably higher for Tech and growth, following years of outperformance.

However, our forecast also noted that US growth and Tech equities should do fine this year, which few agreed with in early April when these categories led the markets lower amid rampant talk of worse to come. But now, even lagging US equities appear poised for a good year, with the correction having reset sentiment much lower everywhere.

Political uncertainty has already eased from the year's start and its peak in April, especially with President Trump's signature budget bill passing in early July. Markets are once again adapting to this administration's unusual style.

Inflation is unlikely to resurge, thanks to subdued money supply growth. US M4, the broadest measure, rose 3.9% y/y in May, in keeping with the low-inflation years pre-COVID.[xi] M2, while accelerating after very slow growth in 2024 (and contraction before that), is far off February's 2021's peak rate above 25% y/y. At 4.5% y/y in May, it too matches pre-COVID trends.[xii] Yes, many still see tariffs as a threat. But the little data we have post-implementation doesn't show much effect on prices, which makes sense: Most American consumption is services, and tariffs don't even affect all goods. Even then, not all companies pass along tariffs to consumers in full (some use other methods of offsetting costs) and not all companies see full tariff charges.

THE TARIFF SCENARIOS

In April, we presented three tariff scenarios—legal and enforcement issues' hindering them, dealmaking, and coordinated retaliation. The first two would be bullish, with tariffs biting less than the worst-case scenario many envisioned, while the third could be materially bad. Since then, a bullish fourth scenario has formed: Other nations easing commerce outside the US. While uncertainty lingers, the bullish scenarios increasingly appear in pole position (in some form or combination), with a deepening trade war looking distant. While we won't reiterate all aspects of these scenarios here, here is an update on events since our Q1 Review.

xi Source: Center for Financial Stability, as of 07/08/2025.

xii Source: Federal Reserve Bank of St. Louis, as of 07/07/2025.

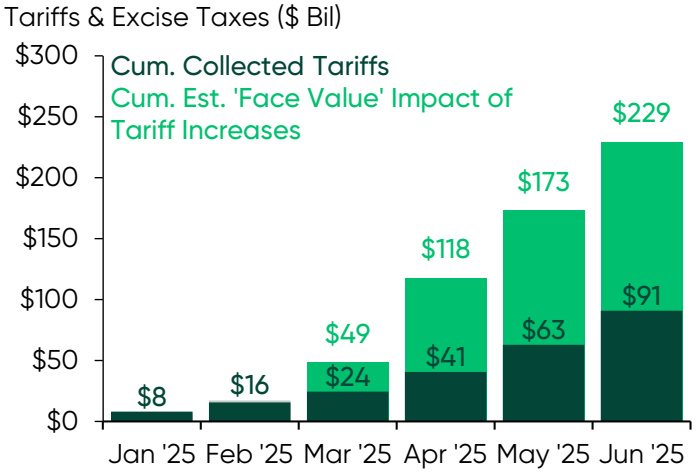
SCENARIO 1: TARIFFS PROVE ILLEGAL AND UNENFORCEABLE

Status: Taking Shape

For tariffs to have the bearish effect many feared, they must stick and be enforced. We told you in Q1 legal challenges could upend the broad tariffs on grounds the trade deficit was a "national emergency." While the process is still underway, the US Court of International Trade ruled in late May that Trump overstepped his authority in attempting to enact both retaliatory tariffs and the 10% universal levy on emergency grounds. The administration appealed, and tariffs remain in place pending said appeal, which is set to start July 31. We still think this case likely winds up at the Supreme Court and can easily see the tariffs being ruled unconstitutional.

Beyond this, tariff collection continues undershooting estimates, likely in part due to the various mitigation methods we detailed, including transshipping, tariff splitting (to reduce imported goods' value) and more. Chinese export data helps illustrate this: While US-bound exports tumbled the last two months, exports to other Asian nations surged. Meanwhile, exports from many of those Asian nations to America jumped—including a more than 100% rise in Singapore's re-exports to America.[xiii] Hence, year-to-date, the $91 billion in cumulatively collected tariffs is a fairly significant rise.[xiv] But it pales in comparison to the $229 billion worst-case scenario estimate based on the face value of tariffed imports.[xv] (Exhibit 4)

EXHIBIT 4: TARIFF COLLECTION YTD VERSUS WORST CASE



Source: Customs and Border Protection, Fisher Investments Research, as of 07/03/2025.

SCENARIO 2: DEALMAKING GALORE

Status: Taking Shape, With Caveats

This scenario envisioned Trump using "Liberation Day" tariffs as negotiating tools to further open markets. Talk of deals ran wild, especially with Trump delaying tariff implementation first to July 9, then August 1 (and possibly beyond), all to facilitate negotiations.

To date, four "deals" have arrived: the UK, China, Vietnam and Indonesia. Britain went first, with an agreement to mitigate tariffs' effects on British autos and US steel in return for buying more US goods. Yet the 10% universal tariff remains, with further talks needed to strike a broader deal. China initially retaliated, then struck a temporary deal to lower bilateral tariffs from triple-digit rates while talks continue. But it expires August 12, and levies remain far higher than a year ago.

xiii Source: Statistics Singapore, as of 06/15/2025.

xiv Source: US Customs and Border Protection, as of 07/03/2025.

xv Source: Fisher Investments Research, as of 07/03/2025.

Vietnam negotiated a deal for 20% tariffs on all US-bound imports, below Trump's threatened 46% but well above rates a year ago. Ditto for Indonesia, which got 19% rates. So, while deals are happening, they aren't exactly creating freer trade. They are better than feared in April but not a free-trade flurry. Perhaps these deals are a prelude to broader arrangements. But we can weigh only those actually struck at this point.

SCENARIO 3: COORDINATED RETALIATION

Status: Few Signs This Is Happening

In April, we couldn't dismiss retaliation. China already had fired back. Negotiations with the EU, Canada and Japan looked fraught. While differences remain, China and America have cooled tensions with their deal-to-make-a-deal. Canada continues negotiating, with Prime Minister Mark Carney ditching a Digital Services Tax targeting US firms in June. The EU and US are talking, too. There is little retaliation to report beyond rumors and threats (e.g., Brazil) and no sign of coordination, which may be mere negotiating ploys.

NEW SCENARIO 4: NON-US ACTIONS FREE GLOBAL TRADE FURTHER

Status: Early Days, but Taking Shape

Another possible scenario has emerged since Q1's Review: Non-US nations banding together not to retaliate, but to boost trade among themselves. In mid-April, the UK slashed tariffs on 89 products *unilaterally*. It then struck a trade pact with India and reached a deal with the EU on outstanding Brexit issues in mid-May.

Canada eased provincial rules hampering domestic trade and fast-tracked major infrastructure projects. It is restarting trade talks with Britain and India, and the EU is talking with Canada, Australia, India and Japan. Other examples abound. While these are works in progress, the trend suggests greater cooperation could be the world's response to US tariffs—a big, underappreciated plus.

WHAT ABOUT MANUFACTURING RETURNING TO AMERICA?

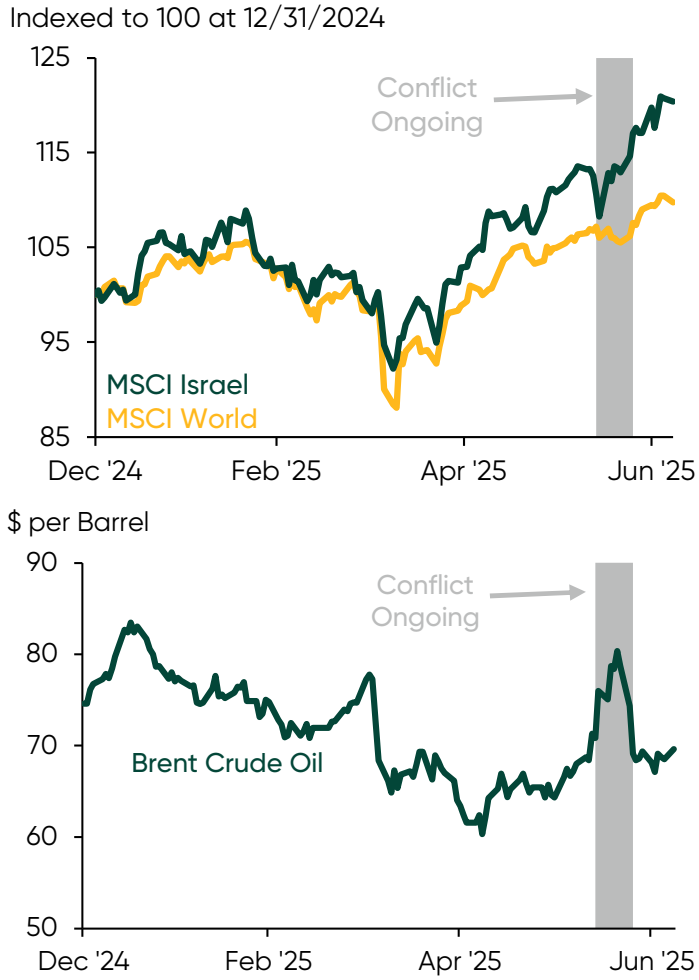
Another question many ask relative to tariffs: Is manufacturing returning to America—and are we planning for that in portfolios?

We doubt such a renewed focus on manufacturing is likely. But regardless, given the permitting process, construction timeframes and more, it would likely take years and years to see it. This is much further out than markets weigh. And, importantly, equities care little about *where* something is made. They care about profits and revenue. Positioning portfolios for manufacturing revival risks being premature at best and wrong at worst.

REGIONAL CONFLICT DIDN'T SINK EQUITIES

In June, regional conflict returned as Israel struck Iran's nuclear facilities—and the US got involved days later. Despite headline warnings over oil price spikes and geopolitical uncertainty, equities barely blinked and oil prices retreated quickly. By June 24's ceasefire, global *and Israeli* equities exceeded pre-conflict levels. Brent crude oil, the global benchmark, was below it. (Exhibit 5, see next page) This is the latest example illustrating regional war rarely moves markets materially.

EXHIBIT 5: THE 12-DAY WAR BARELY SWAYS EQUITIES AND OIL



Source: FactSet, as of 07/08/2025. MSCI World and MSCI Israel with net dividends, Brent crude oil, 12/31/2024 – 07/07/2025.

THE 'WEAK' DOLLAR

The US dollar weakened steeply in 2025's first half, which some dub its "worst start to a year ever," arguing the -7.5% slide against a broad trade-weighted currency basket shows deteriorating confidence in the greenback. But as we often counsel when headlines hype volatility, it is important to zoom out. 2025's slide merely reverses a late 2024 surge, putting the dollar at levels many deemed too strong for years. (Exhibit 6)

In the long run, currencies always trade in pairs and major ones simply waver, much as this year's weak dollar reverses prior strength. Beyond this, all the feared effects of currency swings are easy to overstate, especially since executives are very well versed in hedging for such moves.

EXHIBIT 6: THE DOLLAR'S SLIDE IN PROPER PERSPECTIVE

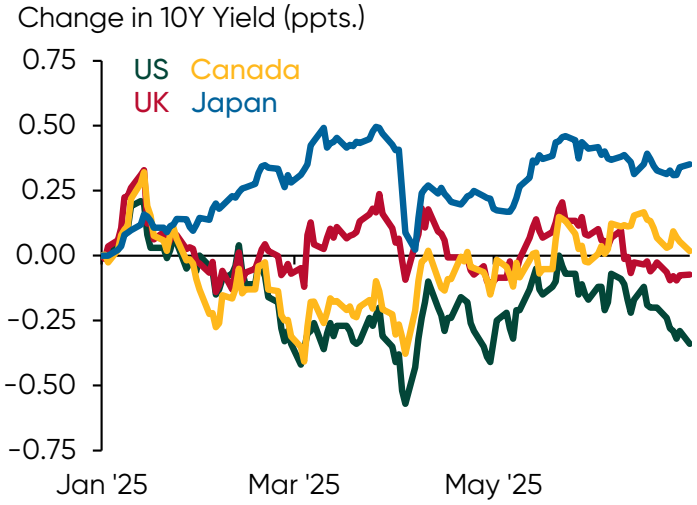
Source: FactSet, as of 07/08/2025. Federal Reserve Trade-Weighted US Dollar Index (Broad), 12/31/2014 – 07/07/2025.

ZOOM OUT ON RATES, TOO

From Britain to Canada, and the US to Japan, interest rates' wobbles similarly stole headlines in Q2. Many tie these moves to debt and deficits, like chatter over the US budget, passed in July. But this, too, looks correction-like. Zooming out is the antidote to these fears, too. Many hyped allegedly "weak" results at May US and Japanese long-term bond auctions as signs deficit fears were eroding demand. Yet those auctions weren't as weak as feared and later sales went smoothly, undercutting the narrative. In all, US 10-year yields finished Q2 literally 1 basis point (0.01 percentage point) higher than at the quarter's start.[xvi] UK yields fell 18 basis points.[xvii] Japan's yields similarly fell 8 basis points.[xviii] Canadian yields rose, but only 24 basis points.[xix] Moreover, none of these show sharp changes year to date. They are wiggling in a tight range, as we expected to start 2025. (Exhibit 7)

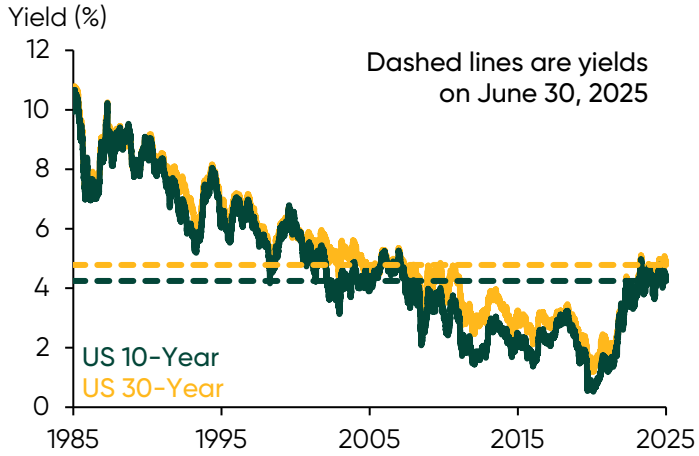
Furthermore, for all the talk of rising US long rates lately, a broader view of 10- and 30-year yields shows they are neither spiking nor particularly elevated by historical standards. (Exhibit 8)

EXHIBIT 7: YIELD MOVES YTD THROUGH Q2



Source: FactSet, as of 07/14/2025.

EXHIBIT 8: US LONG RATES IN PERSPECTIVE



Source: FactSet, as of 07/14/2025.

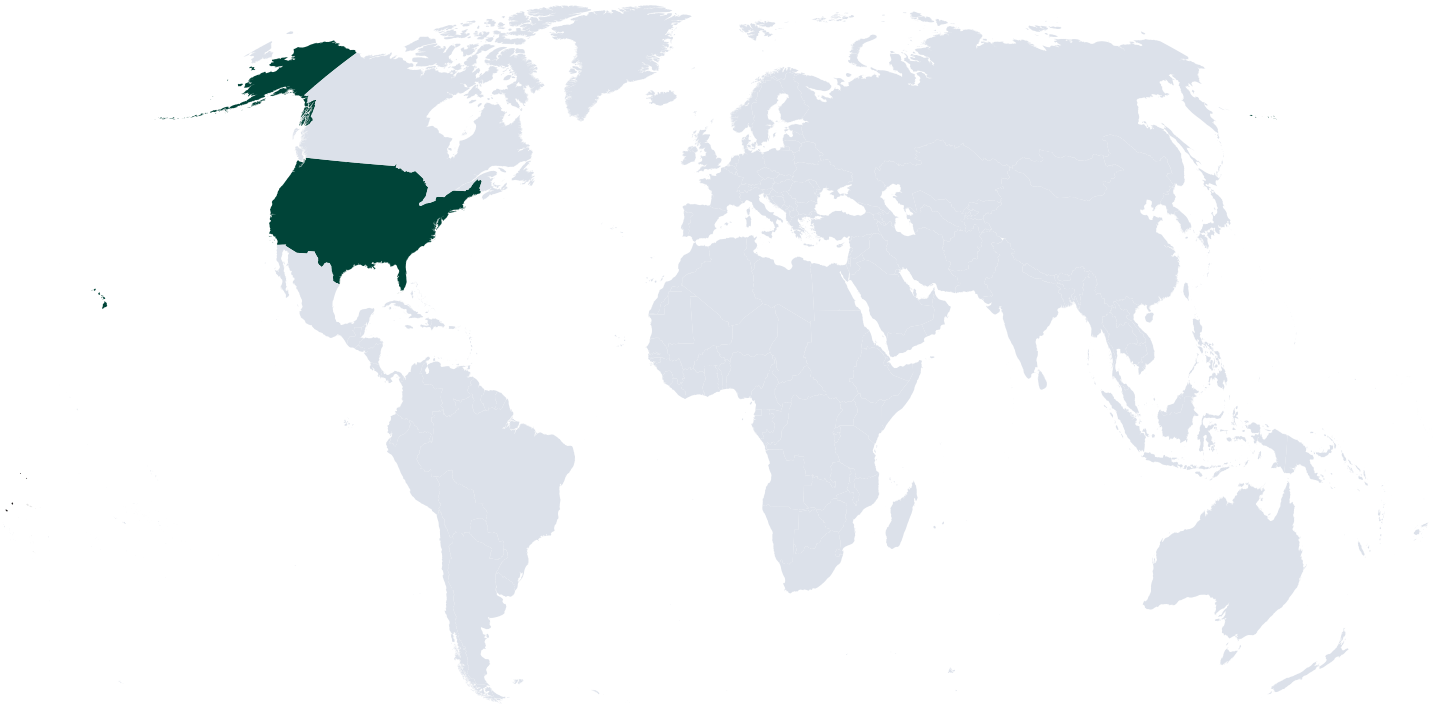
xvi Source: FactSet, as of 07/08/2025. US 10-Year Treasury yield change, 03/31/2025 – 06/30/2025.

xvii Ibid. UK 10-Year Gilt yield change, 03/31/2025 – 06/30/2025.

xviii Ibid. Japan 10-Year JGB yield change, 03/31/2025 – 06/30/2025.

xix Ibid. Canada 10-Year Government Bond yield change, 03/31/2025 – 06/30/2025.

UNITED STATES **COMMENTARY**



ON THE BIG BEAUTIFUL BILL

Please note: Our political commentary is intentionally nonpartisan, favoring no party nor any politician. Our analysis focuses on legislative developments' potential economic, market and personal finance implications.

After months of House and Senate deliberation, President Donald Trump signed the One Big Beautiful Bill Act (OBBBA) July 4. The budget bill, passed on partisan lines, has stirred both celebration and consternation. Here we set all that aside, looking first at what the bill contains—and then at potential market reactions. On that front, we think this bill's effects are likely much smaller than many see.

KEY PROVISIONS IN THE OBBBA

The OBBBA's main feature extends the status quo: making 2017's tax cuts, previously set to expire this year, permanent. It also temporarily lifts state-and-local tax (SALT) deductions from $10,000 to $40,000 (with phase-outs for earners over $500,000) and creates temporary tax deductions for seniors, tipped workers, those working overtime and car buyers. This isn't quite the blanket "no tax on [Social Security, tips, overtime and car loan interest]" touted earlier. But, for example, seniors 65 and older earning up to $75,000 (and joint filers up to $150,000) may deduct an extra $6,000 per person until the provision sunsets in 2028.

Beyond such measures, the OBBBA also slashes spending on various programs, including Medicaid and renewable energy credits, while expanding others such as homeland security and national defense. Most of this was widely expected—old news to forward-looking equities, which began pre-pricing likely legislation on the campaign trail last year. It also lifts the debt ceiling by $5 trillion, although this is always a nonstarter for markets, as we have written many times.

What *isn't* in the OBBBA is also notable. Earlier drafts eliminated the Public Company Accounting Oversight Board, prompting some alarm over audit and financial statement quality (though the SEC was preparing to take over its duties). But the Senate parliamentarian found this provision didn't qualify under the budget reconciliation rules used to pass the bill by a simple majority vote. The House version also contained a provision letting the White House enact a tax on foreign investors whose home nation attempted to enforce the global minimum corporate tax on US firms. But the Senate removed it after international agreements largely eliminated the perceived need. With these out and the balance widely discussed before passage, there is little in this bill markets haven't already weighed. The provisions' effect looks small.

OBBBA DEBT PERCEPTIONS DON'T MATCH REALITY

While the specifics don't have market pundits up in arms, many worry over the long-term debt estimates. The Congressional Budget Office (CBO), the official scorekeeper on such matters, forecasts the bill will add a cumulative $4 trillion (including interest costs) to the nation's debt over 10 years. Moreover, if Congress were to extend or make permanent temporary provisions—like higher SALT deductions—CBO estimates the 10-year cost could hit $5.4 trillion. To many, these figures seem astronomical and stir fears of bond market trouble.

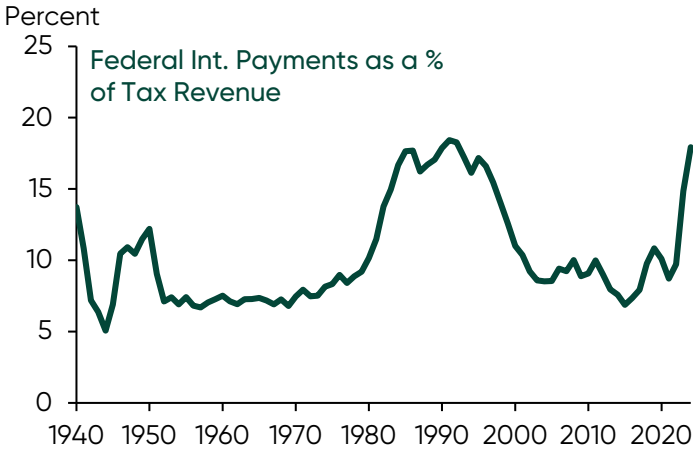
SPREAD OUT OVER 10 YEARS, DEBT PROJECTIONS ARE RELATIVELY MODEST

Some coverage cast this as adding $4 trillion to the deficit, implying that much new debt annually. But it is cumulative—the projected new debt *over the next decade*. $400 billion a year, on average, would be easily digestible for Treasury markets. Net debt held by the public—currently at $29 trillion—rose $1.9 trillion in 2024. Benchmark 10-year Treasury rates wobbled in the same roughly 3.6% – 5.0% range they are in today.[xx]

Or take 2020, when publicly held debt soared almost $5 trillion in one year—the high end of the CBO's projections for *the next decade*. That year, the benchmark 10-year rate sank from 1.9% to as low as 0.5%.[xxi] Whatever your view of the borrowing binge, there is little to suggest markets couldn't absorb it.

Numbers in the trillions always sound big, but the absolute amount of debt or deficit isn't the key. Whether government revenues cover debt payments is—which they do, several times over, at a ratio paralleling much of the 1980s and 1990s. (Exhibit 9)

EXHIBIT 9: DEBT PAYMENTS REMAIN AFFORDABLE



Source: Federal Reserve Bank of St. Louis, as of 07/07/2025.

xx Source: FactSet, as of 07/07/2025.

xxi Source: FactSet, as of 07/07/2025.

BESIDES, ANYTHING CAN HAPPEN IN 10 YEARS

Second, the CBO's straight-line projections are meaningless. Just because it is nonpartisan, doesn't mean its 10-year forecasts are accurate—by its own admission.

Consider CBO revenue projections for 2017's Tax Cut and Jobs Act (TCJA). At the time, it claimed the bill would reduce federal revenue by -$1.0 trillion over 10 years from a hypothetical scenario in which the TCJA wasn't passed.[xxii] But, years later, the CBO reported: "Nominal receipts from fiscal years 2018 to 2024 were $1.5 trillion (or 5.6 percent) greater than the total of $27.0 trillion that CBO projected for that period in April 2018."[xxiii]

Just as instructive is *why* revenue projections undershot:

> "CBO currently estimates that the primary reason for the higher revenues is the burst of high inflation that began in March 2021. That inflation contributed roughly $900 billion to the $1.5 trillion difference. An increase in real economic activity, especially in the later years of the period, also contributed to the higher revenues, adding roughly $700 billion to the difference. Customs duties from new tariffs contributed an additional $250 billion. Other factors, including subsequent legislation, partially offset those first three factors."

In other words, factors no one can know beforehand—"high inflation" and "real economic activity"—render straight-line assumptions and wild guesses.

That is before you even get to "subsequent legislation" from the next Congress. America rarely keeps tax policy unchanged for a full decade. The OBBBA undid items in past budget bills. Other legislation could easily undo it down the road.

Since no one—the CBO nor anyone else—has any clue what will happen politically over the next decade, the idea its budget forecasts will stay unchanged is hardly credible. This is why we say forecasts are merely opinions. It is reckless to treat them like truth. Markets know this—likely why bond yields didn't react materially to OBBBA's passage.

INFLATION FURTHER MITIGATES ANY IMPACT

Also, as the CBO's postmortem hints, inflation defrays debt considerably. Inflation is awful for taxpayers and households. But it is great for the US government, reducing the real value and servicing cost of the entire outstanding debt stock. This is because US debt is denominated in "nominal" or current dollars. Inflation erodes the value of those dollars over time—shrinking the real value of America's debt load accordingly.

Since COVID struck, CPI rose 24.0%.[xxiv] Arguably, even that understates the real effect. At 2020's start, the Federal government had $17 trillion in publicly held debt. But inflation since then cut that by -$4 trillion in real terms. Just last year, US debt rose $1.9 trillion, but CPI rose 2.9% y/y, trimming 2024's $27 trillion in debt, adjusted for inflation, by -$780 billion.[xxv]

Not only does inflation mitigate repayment in real terms, it also boosts revenue. Nominal US GDP is $30 trillion.[xxvi] If inflation runs 2% annually and real GDP grows 2.5%—below their respective historical averages of 3.5% and 3.2% since 1948—then nominal GDP would expand 4.5% per year or $1.4 trillion.[xxvii] This would dwarf the CBO's 1.4% – 1.8% (around $400 – $550 billion) annual projected debt increase from the OBBBA.

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xxii "The Budget and Economic Outlook: 2018 to 2028," Staff, CBO, April 2018.

xxiii "Additional Information About the Effects of Expiring Provisions of the 2017 Tax Act in CBO's Baseline Projections," Phill Swagel, CBO, 12/04/2024.

xxiv Source: US Bureau of Labor Statistics, as of 06/11/2025.

xxv Ibid.

xxvi Source: US Bureau of Economic Analysis, as of 06/26/2025.

xxvii Source: Federal Reserve Bank of St. Louis, as of 07/07/2025.

Notice what this entails. Given the government's tax take stays about the same percentagewise—which the OBBBA enshrines—in addition to the -$780 billion inflation effect, tax revenue rose some $250 billion.[xxviii] Subtract those, and 2024's $1.9 trillion of added debt falls even further to $870 billion. More than half the supposed gargantuan flow of red ink is thus dissolved.

Thanks to relatively modest price increases, the cumulative rise in nominal debt from the CBO's deficit projections will be smaller than the reduction in real debt. Adjusted for inflation, US debt is much more manageable than many appreciate.

DEBT ISN'T INHERENTLY NEGATIVE FOR EQUITIES

The optimal debt level—or range—for the US or any other entity isn't zero. It is when its marginal borrowing cost just equals its marginal return on assets. More debt is good if America's return on assets exceeds its borrowing cost.

So, is this the case? The average interest rate for all US debt is about 3.3%.[xxix] The US's return on assets can be estimated by dividing total income (GDP) by total assets. In Q4, nominal GDP was just under $30 trillion annualized.[xxx] America's total assets: $314 trillion.[xxxi] America's return on assets, therefore, yields approximately 9.4%—nearly three times its borrowing cost.

To be clear: We aren't advocating a debt-fueled spending binge. Public spending can interfere with private sector capital allocation and create inefficiencies. We are solely arguing there are zero signs, despite the big raw numbers, that America's debt is an economic calamity set to wreak havoc on equities. While hard for headlines to fathom, markets know the score. If debt projections were truly problematic and crisis-inducing, long-term interest rates would be far higher than they are now: below average historically and trading in a fairly narrow range.

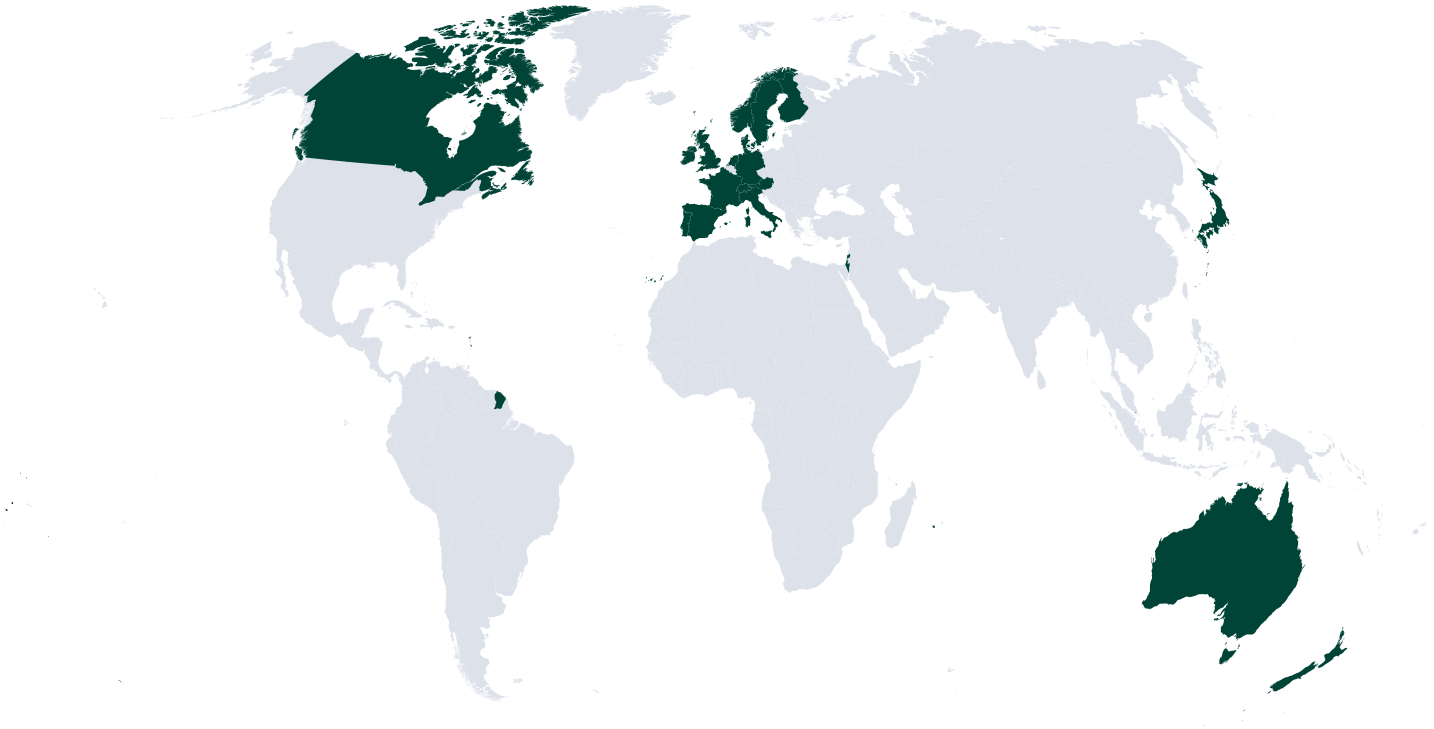
xxviii "How I Learned to Stop Worrying About the National Debt – Even Though It's $35 Trillion," Ken Fisher, *New York Post*, 11/25/2024.

xxix Source: US Treasury, as of 06/30/2025.

xxx Source: US Bureau of Economic Analysis, as of 06/26/2025.

xxxi Source: Federal Reserve and S&P Global, as of Q4 2024.

GLOBAL DEVELOPED EX-US **COMMENTARY**



FACTORS FUELING NON-US LEADERSHIP

Non-US equities led again in Q2 and remain far ahead of US equities year to date, up 19.0% versus the S&P 500's 6.2%.[xxxii] While US markets recouped some ground since late-April, this is likely a byproduct of US equities getting hammered hardest during the correction. What falls the most usually bounces sharpest during the initial recovery. Some project big US outperformance looking forward but miss key points. Not only is sentiment still worse in Europe and Asia, creating a big wall of worry, but economic drivers favoring value equities—Europe's bread and butter—are stealthily improving. Chief among them: the steepening yield curve.

THE STEEPENING GLOBAL YIELD CURVE

When the yield curve inverted in late 2022, nearly every professional noticed. Equities had reached their low in that year's shallow bear market days earlier. Recession forecasts, already widespread, ran wild on inverted curves' recession-predicting prowess. Bearishness abounded as a result. When the US and global economies kept growing—and equities rallied despite inversion lasting through 2024—everyone moved on. Now, with no one looking, it is steepening.

We have previously noted that the inverted yield curve can usually mean trouble, but it could also be a misfire. To know for sure, you must take a deeper look beneath the surface. But few did this with the yield curve. Most seemingly forgot or discarded it, not bothering to see *why* inversion was a false signal. This gives it power now, in our view.

xxxii Source: FactSet, as of 07/07/2025.

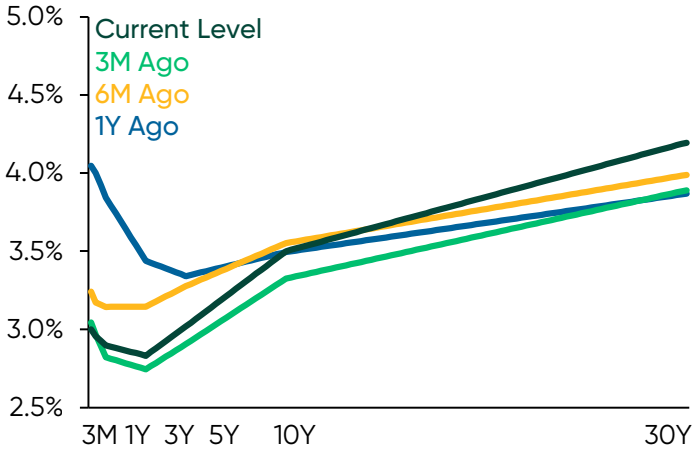
The curve traditionally works because it predicts bank lending by approximating "net interest margins" on new loans—banks' profit margins on issuing credit. Banks borrow at short rates, lend at long rates and profit off the spread. A steep curve renders bigger profits and more lending. Flat curves shrink profits, slowing lending. Inverted curves zap profits, which can shrink lending. Because bank lending creates most new money, falling lending generally means monetary contraction, siphoning economic fuel. This is why inversion often precedes recession.

This time, lending continued. While Fed rate hikes normally raise banks' funding costs, in 2022, banks had huge stockpiles of cheap deposits thanks to COVID policy responses and lockdowns' psychological effects. People hoarded cash, craving stability in an uncertain world. In 2020, US bank deposits ballooned 20.8% y/y, spiked another 11.7% in 2021—and remained elevated through 2022 and beyond.[xxxiii] The trend held across the developed world, all at super-low deposit rates, initially a small fraction of one percent. Therefore, banks kept lending profitably, money supply stayed healthy and economies grew.

Now the curve is positive again, thanks to rate cuts and rising long rates—also widely feared, making this extra-bullish. Because people disregarded the curve, its steepness is an unseen positive, poised to stealthily boost growth—especially outside the US.

While most traditionally focused on the US curve, we have long used a global curve, weighing regions according to their share of developed-world GDP. As Exhibit 10 shows, its spread jumped from -0.55 percentage point (ppt) a year ago to 0.50 ppt, a swing of over 1 ppt. Most of this comes from Europe and Asia, while the US's curve—though improved—remains flattish. (Exhibit 11) Tailwinds are stronger abroad.

EXHIBIT 10: THE STEEPENING GLOBAL YIELD CURVE



Source: FactSet, as of 07/07/2025.

EXHIBIT 11: STEEPER OUTSIDE THE US

Region	Current 10Y	Current 3M	Current Spread	Spread 1Y Ago
Global Ex. EM	3.50%	3.00%	0.50%	-0.55%
US	4.35%	4.42%	-0.07%	-1.01%
Europe Ex. UK	2.89%	1.86%	1.03%	-0.47%
UK	4.55%	4.20%	0.35%	-0.99%
Japan	1.45%	0.44%	1.01%	1.07%

Source: FactSet, as of 07/07/2025.

To us, it is no coincidence steeper curves outside the US parallel non-US equities' leadership. Not only do they boost economic growth overseas, but steep curves traditionally benefit value equities most. Growth equities can leverage their size and balance sheets tap capital markets, but value equities depend more on bank lending to expand. Hence, when yield curves are flattish, value generally lags while growth equities shine. But steep curves shower value equities with the capital to fuel growth and earnings, often pumping outperformance.

While growth equities abound in the US, value dominates Europe. As Exhibit 12 shows, Europe's top four sectors—over half of its market cap—are value-heavy (see next page). The top two, Financials and Industrials, are utterly trouncing global returns, up 38.7% and 39.2%, respectively. No shock here, considering fatter curves directly boost bank profits and funnel piles of cash to value-rich Industrials.[xxxiv]

xxxiii Source: US Federal Reserve, as of 05/14/2025. Assets and Liabilities of Commercial Banks.

xxxiv Source: FactSet, as of 07/07/2025. MSCI Europe Industrials and MSCI Europe Financials returns with net dividends, 12/31/2024 – 06/30/2025.

Meanwhile, in the US, over 40% of market cap is in the growth-heavy Tech and Communication Services sectors, home to big Tech-like companies. Consumer Discretionary—heavy with growth-oriented e-commerce firms—also has a large weighting, while America's Financials sector pales in comparison to Europe's.

EXHIBIT 12: EUROPE'S VALUE TILT, TOP SECTOR WEIGHTS

US		Europe	
Tech	33.1%	Financials	22.7%
Financials	14.0%	Industrials	19.2%
Consumer Discretionary	10.4%	Health Care	13.5%
Communication Services	9.8%	Consumer Staples	9.8%

Source: FactSet, as of 07/16/2025. Top 4 S&P 500 and MSCI Europe Index sector weights on 06/30/2025.

Given our forecast for European and value outperformance, we have increased our portfolio emphasis on these areas while paring US and growth exposure. As these trends continue playing out, portfolios should be well positioned. And while the steeper yield curve and America's tariff headwinds are big factors affecting relative returns, they aren't the sole drivers.

THE EUROZONE'S ENGINE IS REVVING UP

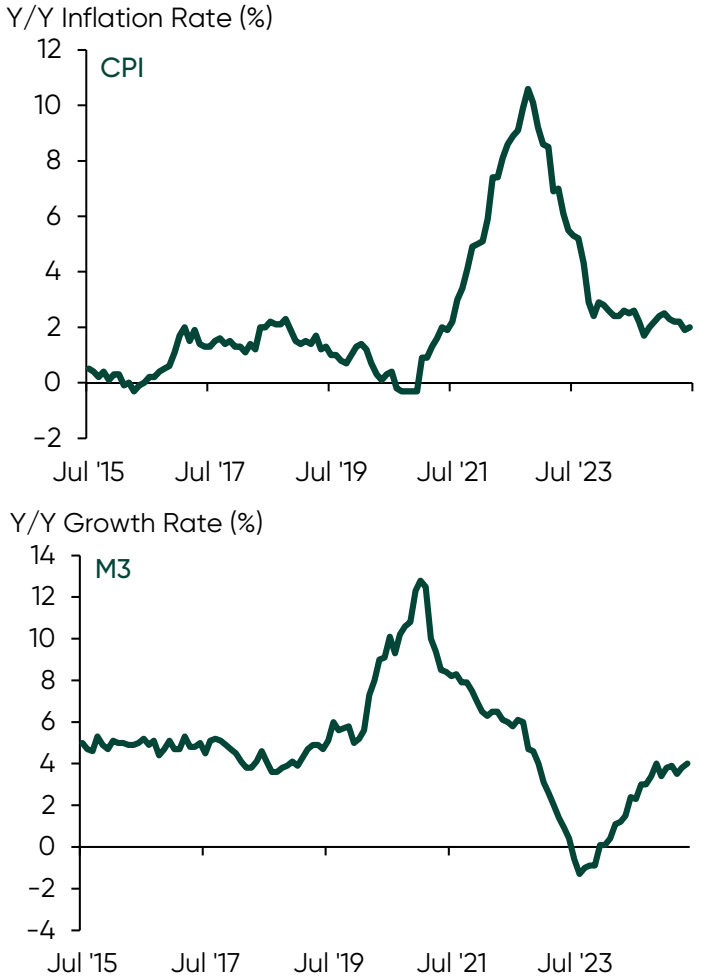
Calling eurozone sentiment dim would be an understatement. Southern nations remain colored by the early 2010s' debt crisis and double-dip recession, cementing perceptions they lurch from bailout to bailout with no growth. Germany is now considered by some as Europe's alleged "sick man" with two straight annual GDP declines. Political instability fuels global views of a stagnant bloc.

But these viewpoints are years old, long since being priced in. Markets don't look backward, they look forward, pricing in the high likelihood things shape up better than today's dreary expectations.

Headlines say Germany's stagnation will soon spread regionally, as French growth collapses under high debt and Italy and Spain's tourism booms fade, revealing hollowed-out local economies. But France's debt is a political problem, not an economic one, as interest costs remain benign historically. Meanwhile, Q1 GDP rebounded from a one-off contraction, led by rebounding business investment. Consumer spending stumbled, but retail sales' swift growth in March and April suggests it was a temporary speedbump. Spain and Italy's services purchasing managers' indexes remained in expansion through June. If hospitality alone were driving growth, a majority of businesses nationwide wouldn't be reporting expansion.

The steepening yield curve should remain a big tailwind. Central bank moves can defy prediction and logic, but the European Central Bank has latitude to cut rates further and has signaled it wants to do so. Regional inflation remains tame and money supply is growing modestly. (Exhibit 13, see next page) The inflation war is over, rendering high rates unnecessary.

EXHIBIT 13: EUROZONE INFLATION AND MONEY SUPPLY



Source: FactSet, as of 07/10/2025. Headline CPI, July 2015 – June 2025 and M3 money supply, July 2015 – May 2025.

Politics are also more benign than portrayed. France's government nearly collapsed for the second time in a year in late June over stalled pension reforms, but this noise obscures the simple reality of bullish gridlock. Uncertainty is elevated for now, but as it fades, gridlock's traditional tailwinds should reign. When a government can't pass anything, it can't create winners and losers or drive risk aversion through sudden change.

The Netherlands, whose government did collapse in Q2, has shown this time and again. Collapses, snap elections and multi-month government formation process are increasingly normal there, as are fractious coalitions featuring populist parties. Yet Dutch equities are up 20.6% year to date, more than doubling global returns.[xxxv]

BULLISH BRITAIN ISN'T BRITTLE

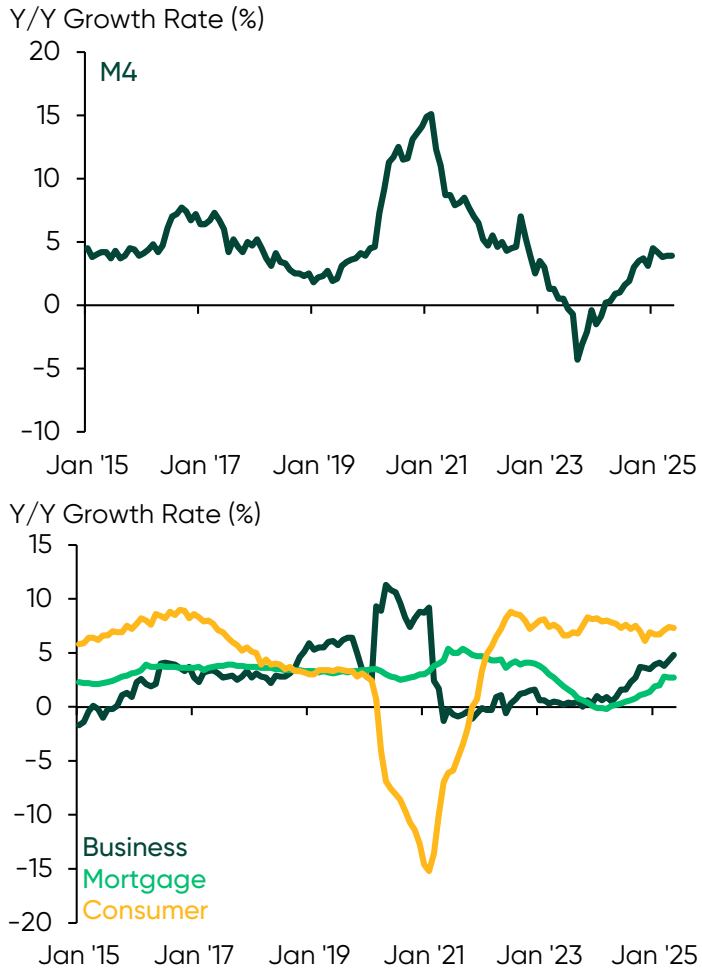
The UK also has a big wall of worry, with shaky economic data fueling pessimism despite UK equities' hitting all-time highs. Monthly GDP wobbled in April and May, but this looks mostly like a pothole after tariff fears pulled exports and production into Q1. Meanwhile, services—the bulk of UK GDP—are proving resilient, flipping from slight contraction to growth in May. This recovery helped GDP's contraction ease from -0.3% m/m in April to -0.1%, and overall, April's employer NIC hikes don't appear to be harming growth as widely feared.[xxxvi] Meanwhile, trade recovered in May, with exports and imports up nicely—including exports to the US.

Inflation accelerated, but largely due to household energy's price "cap" stepping up. It falls again in July though. Inflation fears are running hot, tied to worries businesses will pass recent tax hikes to customers, but money supply growth has slowed lately. The current growth rate fanned fears of *too low* inflation a decade ago. (Exhibit 14, see next page) Here, too, the Bank of England has room to cut rates further, adding to the yield curve's steepness, which is already helping loan growth.

xxxv Ibid. MSCI Netherlands return with net dividends, 12/31/2024 – 06/30/2025.

xxxvi Source: Office for National Statistics, as of 08/07/2025.

EXHIBIT 14: UK MONEY SUPPLY AND LENDING



Source: Bank of England, as of 07/10/2025. M4 money supply (ex. intermediate OFCs) and lending to private non-financial corporations, consumers and home buyers, January 2015 – May 2025.

Political sentiment is also too dour. After Prime Minister Keir Starmer and Chancellor of the Exchequer Rachel Reeves' welfare reforms flopped in July, passing in watered-down fashion, analysts speculated about more tax hikes and Reeves' future. A potential wealth tax is the latest fear, and pundits hype every rumor of Reeves' downfall. We think this is all too distant to speculate over now. Reeves' position appeared to solidify in July as she switched focus to cutting red tape in an effort to foster investment and growth, whilst Starmer's removing the Labour whip from the welfare bill rebels appears to be a first step aimed at rebuilding political capital. Moreover, if economic data improves, the math calling for tax hikes presently may look different than feared now.

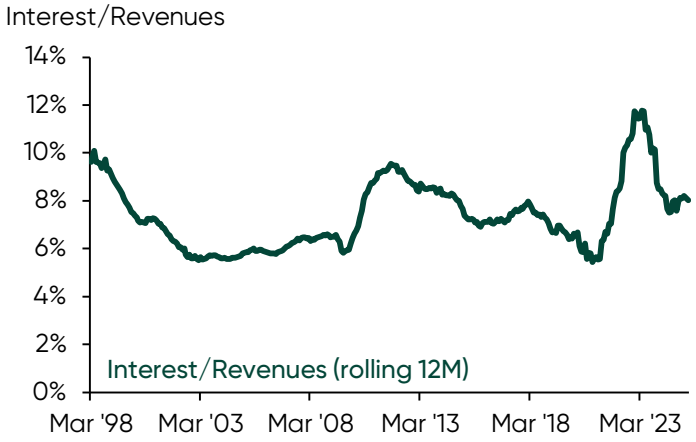
As in France, UK public finances are a political issue more than an economic one, stemming from the "Golden Rule" adopted in 1998, which requires fiscal policy to target a balanced budget within five years. The Office for Budget Responsibility's (OBR's) economic forecasts have become the arbiter for this, essentially forcing taxes and spending to shift with the changing outlook. In recent years, this has meant governments from both parties raising taxes to keep projected deficits in line, as well as sharp market volatility whenever politicians have mooted curbing the OBR's role. The irony here is that the Golden Rule hasn't actually fostered a sustained budget surplus. Rather, it seems to have prompted chancellors to shift taxes and spending just enough to keep five-year forecasts in compliance, delaying true change time and again. Meanwhile, the government runs persistent deficits.

However, there is a growing awareness in UK political ranks that the fiscal rules keep taxes and spending on shifting sand, which increases uncertainty and discourages risk taking. Amending the rules, which Reeves has hinted at, would raise some economists' hackles (as it did when former Prime Minister Liz Truss attempted a different approach). But it could reduce uncertainty over time—a potential positive no one talks about.

In the meantime, the UK doesn't appear to be on the verge of a fiscal crisis. Whilst debt has indeed grown in recent years, so has tax revenue as growth and inflation lifted the tax base. As a result, debt service costs are down relative to tax revenues after spiking briefly in late 2022 and early 2023 due to faster inflation's effects on index-linked Gilts. They now sit about where they did in early 2018, even though UK debt has risen by about £1 trillion since then.[xxxvii] (Exhibit 15, see next page)

xxxvii Ibid.

EXHIBIT 15: UK DEBT REMAINS AFFORDABLE



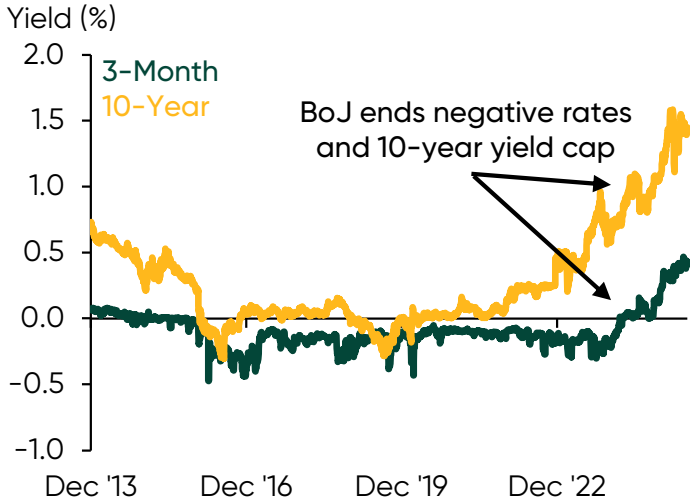
Source: Office for National Statistics, as of 07/08/2025.

Accordingly, whilst headlines focus on every wiggle in UK bond markets, we think this is just normal short-term volatility—sentiment-fueled swings. If UK debt were problematic, Gilt yields would be far higher than US Treasury yields. Instead, they move largely parallel, and long-term Gilt yields are actually flattish year to date. Equities, too, signal this isn't a problem. Debt talk is neither new nor surprising, and UK equities are clocking new highs despite them. We think debt fears simply extend the UK's wall of worry—a bullish signal, in our view.

JAPAN RETURNS TO NORMAL

Japan is hiking rather than cutting rates. But Japan's yield curve has steepened, too, because it represents monetary policy's return to normal after years of negative short rates and capped long rates. Since the Bank of Japan ended negative rates and "yield curve control" 10-year rate caps in late March 2024, its yield curve spread widened by 30 basis points. (Exhibit 16) Long rates rose more than short rates—a return to normal. Banks now have more latitude to fund economic growth.

EXHIBIT 16: JAPAN'S RETURN TO MONETARY SANITY



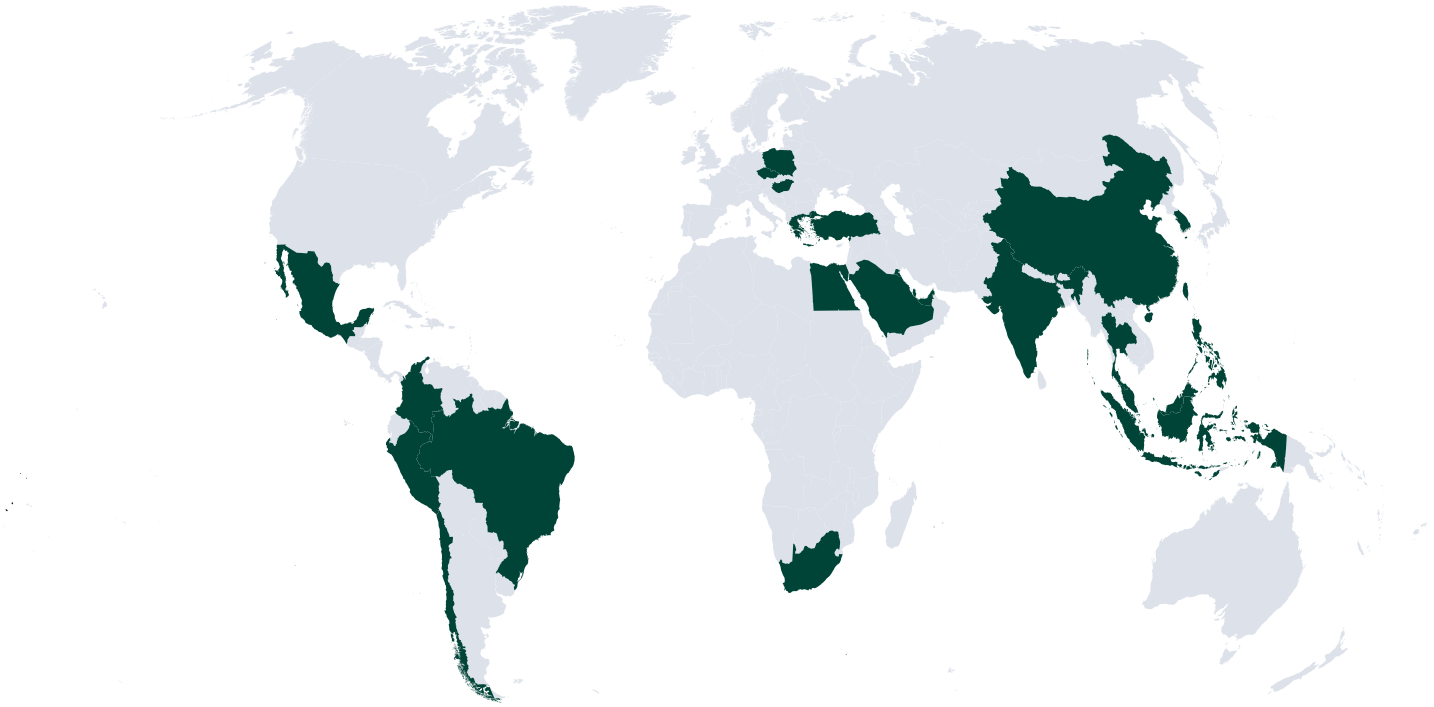
Source: FactSet, as of 07/08/2025. Japanese 3-month and 10-year bond yields, 12/31/2013 – 07/07/2025.

Japan's steepening yield curve has coincided with a notable economic uptick. After shrinking three straight quarters through Q1 2024, GDP grew solidly through the rest of the year. While it contracted -0.2% annualized in Q1 2025, this stemmed chiefly from falling government spending.[xxxviii] Household consumption grew 0.5% annualized, while business investment jumped 4.4%.[xxxix] Fast-rising imports also hint at improving domestic demand. Monthly data since are complicated by tariff fears pulling a lot of international trade into January and February, leaving a bit of a fracture in their wake—a factor skewing springtime trade and industrial production readings globally. But retail sales and other domestically-oriented measures appear to be on solid footing, while inflation is slowing again.

xxxviii Source: FactSet, as of 07/08/2025.

xxxix Ibid.

EMERGING MARKETS **COMMENTARY**



EMERGING MARKETS POLITICAL UPDATE

NEW KOREAN PRESIDENT'S CORPORATE REFORMS: SAME AS THE FORMER'S?

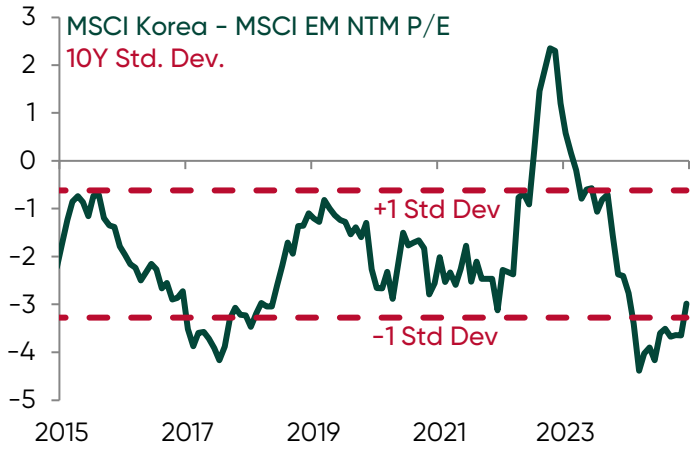
As polls predicted, South Korean voters elected former opposition leader Lee Jae-myung as president June 3. This capped months of political turmoil following President Yoon Suk Yeol's December martial law decree and subsequent impeachment. With Lee's center-left Democratic Party also controlling the unicameral National Assembly, hopes for corporate reform are rising, headlined by the new administration's push for promotion to a developed market from its current Emerging Markets status (a process MSCI confirmed it continues monitoring in its annual Market Classification Review, announced in June).

Days after the election, for example, Lee moved to strengthen Korea's Fair Trade Commission and bulk up staffing, presumably for more active antitrust enforcement. Then on July 3, the National Assembly revised the Commercial Act, effectively holding corporate boards accountable to minority shareholders, not just entrenched business interests—like the families who control South Korea's influential national champion *chaebol* (sprawling family-owned conglomerates). Also in the works: the Online Platform Act to regulate digital services and marketplaces against uncompetitive practices.

But we don't see governance and regulatory measures going much differently than similar proposals under Yoon. While Lee is in a better position politically than Yoon to pass reform, revising the law typically requires a one-year notice period before it can take effect—like with the Commercial Act. In the meantime, *chaebol* can push back, as they have for decades, limiting progress.

So, although falling political uncertainty is a tailwind in South Korea, we do see the possibility of hopes for reform teeing up eventual disappointment. There is also a chance that the recent rally has been fueled purely on negative sentiment and could lose steam as it normalizes. (Exhibit 17) That doesn't appear at hand now, but it is something we are monitoring.

EXHIBIT 17: SOUTH KOREAN SENTIMENT, RELATIVE TO BROADER EMERGING MARKETS



Source: FactSet, MSCI Korea and MSCI EM Price to Earnings (NTM) from 07/01/2015-06/30/2025.

TAIWAN'S SPLIT GOVERNMENT PLAYS HARDBALL

On June 20, Taiwan announced a July 26 recall election for 24 Kuomintang (KMT) lawmakers over severe budget cuts and other controversial measures, potentially swinging the legislature's balance. Currently, the government is split after the Democratic Progressive Party's (DPP's) Lai Ching-te won the presidency last year while the party lost its majority in the 113-member parliament, taking only 51 seats against the KMT's 52 alongside another 8 from its allied Taiwan People's Party (TPP).

Given KMT-TPP parliamentary control, they pushed through legislation that some political analysts characterize as leading to a constitutional crisis.[xl] For one, the Constitutional Court Procedure Act requires 10 of the Constitutional Court's 15 judges to issue rulings versus a simple majority previously. The KMT-TPP coalition passed this knowing 7 of those 15 judges would retire in October 2024—and that it could block Lai's nominations, effectively handcuffing the Constitutional Court and expanding legislative power.

Such "lawfare" seems to be sparking alarm regarding Taiwan's military readiness and ability to conduct foreign policy, including trade negotiations. The KMT and TPP have undertaken "the biggest cut in history" to the budget, including the Ministry of Defense's spending.[xli] And, with many seeing the Trump administration as tying defense partners' military spending to trade talks, the outcome of recalls and any subsequent by-elections' reshaping parliament has investors on edge.

Successful recalls require at least a quarter of eligible constituents participating and a majority of them voting in favor of removing the officeholder. If a lawmaker is recalled, they would be ineligible to run again in by-elections that must be held within three months. Rising uncertainty in the leadup is understandable, but as results become known and the fog clears, we see political headwinds—only one factor among others driving markets—reversing.

xl "Obscured by Geopolitics, Taiwan's Constitutional Crisis Simmers in the Background," Lucy Best, *The Diplomat*, 06/25/2025.

xli "Deep Cuts to Government Budget Spark Widespread Recall Efforts Against KMT Legislators in Taiwan," Ricky Yeh, *The Diplomat*, 01/28/2025.

THAI POLITICAL TURMOIL SWIRLS

Thailand's pro-military Bhumjaithai Party, the second-largest in Prime Minister Paetongtarn Shinawatra's Pheu Thai-led ruling coalition, exited the government on June 18, raising prospects for political instability. Thailand is presently embroiled in a border conflict with Cambodia. So, when former Cambodian Prime Minister Hun Sen leaked a recording of Shinawatra criticizing Thailand's army, domestic political blowback was sharp and Bhumjaithai announced its exit. Given it holds 69 seats in the 500-member House of Representatives, this leaves the remaining coalition with only a slim majority at 261 seats. Furthermore, Bhumjaithai is now seeking a no-confidence vote against Shinawatra.

Adding to the government's woes, the Constitutional Court suspended Shinawatra from her premiership duties on July 1, pending its ethics investigation over the leaked call. Notably, Shinawatra became prime minister 10 months ago after the Constitutional Court dismissed her predecessor, Pheu Thai's Srettha Thavisin, on unrelated ethics charges. During Shinawatra's suspension, Deputy Prime Minister Suriya Juangroongruangkit will helm the government in a caretaker role. This is as public protests mount, demanding Shinawatra's resignation, and speculation swirls over whether other coalition members could defect.

Meanwhile, Thai Finance Minister Pichai Chunhavajira is racing to avert threatened 36% US tariffs set for August 1. How all this resolves remains unclear, but with Shinawatra's approval rating dipping into single digits, it seems unlikely her administration will last.[xlii] While political uncertainty is weighing on sentiment, keep in mind that Thai stocks—and Shinawatra—are no strangers to it, as the military overthrew both her father's and aunt's prior governments.

MEXICO'S RULING PARTY SOLIDIFIES COURT CONTROL

Mexican judicial elections June 1 resulted in the ruling Morena party securing at least six friendly seats in Mexico's nine-member Supreme Court. In a first of its kind for the world, Mexicans voted for about half of all judges—including 1,801 local seats, 881 federal and the Supreme Court—with the other half slated for 2027. Though popular with two-thirds polled in favor of electing judges, the low 13% turnout—with over 20% of those ballots blank or invalid—raises questions over the vote's legitimacy.[xliii] Regardless, most positions went to Morena-vetted candidates, suggesting President Claudia Sheinbaum's party controls the Mexican government's three branches—and three-quarters of its state governorships.

The lack of gridlock and judicial checks raises the risk of government overreach and radical legislation. But for investors, politics is only one factor—and surprises move markets most. Morena's winning nominal control of the judiciary was widely expected—the baseline assumption, given Sheinbaum and her predecessor have long pushed for a vote.

NEW POLISH PRESIDENT PRESERVES STATUS QUO GRIDLOCK

June 1 also saw Poland elect a new president as the nationalist Law and Justice Party's Karol Nawrocki edged out Warsaw Mayor Rafal Trzaskowski of the centrist Civic Platform. It was a closely watched race that many believe is key to whether Prime Minister Donald Tusk's Civic Platform-led coalition government can enact his agenda.

xlii "Thailand Plunges Deeper Into Crisis as Court Suspends Leader," Patpicha Tanakasempipat, *Bloomberg*, 07/01/2025.

xliii "Ahead of Mexico's First-Ever Judicial Elections, Most Mexicans Approve of the Law That Implemented Them," Jordan Lippert and Sofia Hernandez Ramones, Pew Research Center, 05/22/2025.

Since the president has veto power, requiring a three-fifths majority to overrule—which the coalition doesn't have—Nawrocki appears likely to stymie the government's legislative initiatives. This may be frustrating to some, but it wouldn't be much different from previous President Andrzej Duda—an independent allied with Law and Justice. Markets should be fine with such status quo gridlock.

CHINA'S POSITIVELY SURPRISING FIRST HALF

Ever since US President Donald Trump won a second term in the White House last November, fears of an acrimonious trade relationship with China have run wild. Many feared the effects of a trade war on the Middle Kingdom, especially considering slowing economic growth, flagging retail sales, continuing contraction in real estate investment and "deflation." Pundits argue this is a negative backdrop for Chinese equities and world economic activity.

Since January, tariff fears have come true—perhaps on an even larger scale than many anticipated. While early April's trade war and prohibitive 100%+ tariffs proved short-lived ahead of a US-China "deal," the deal expires August 12 and still leaves levies far, far higher than six months earlier. Yet Chinese growth has proven far more resilient than feared. And stocks have climbed on the positive surprise. Through June 30, Chinese stocks are up 17.3% in 2025, outpacing both Emerging Markets' 15.3% and the MSCI All-Country World Index's (ACWI) 10.0%.[xliv] Let us dig into the data to explore how China's economy is coping.

At a high level, China's GDP has accelerated in 2025. After growing 4.8% y/y and 5.0% sequentially in 2024's last two quarters, Q1 2025 posted 5.4% before a slight Q2 downtick to 5.3%.[xlv] Many pundits greeted these data skeptically, arguing the full brunt of the trade war wasn't reflected. There is a chance that is true. But on a sector basis, it is worth acknowledging services—the majority of China's GDP—grew 5.5% y/y in Q2, outpacing headline growth and manufacturing's 5.3%.

While it is possible the data don't yet reflect the full impact of tariffs, there are some caveats to this. When trade tensions spiked in Trump's first term, Chinese firms found workarounds to mitigate the impact. One, some employed transshipping, an illegal practice of sending goods from a Chinese port to another, largely in southeast Asia, where they are relabeled and sent onward to America. Two, they built final assembly or other factories abroad, a fully legal way to reduce tariffs' effects.

Export data through June imply they are once again employing these tactics. Chinese exports to America have tumbled since April 2's Liberation Day tariffs triggered the tit-for-tat trade war, falling -21.0% y/y, -30.1% and -14.6% in April, May and June, respectively.[xlvi] Yet *overall* Chinese exports grew 8.1% y/y, 4.7% and 5.9%, underpinned by huge surges in exports to Thailand, Vietnam, Malaysia and Singapore. (Exhibit 18, see next page) Trade and transit hub Singapore noted that non-oil re-exports to the US rose 64.3% y/y in June.[xlvii]

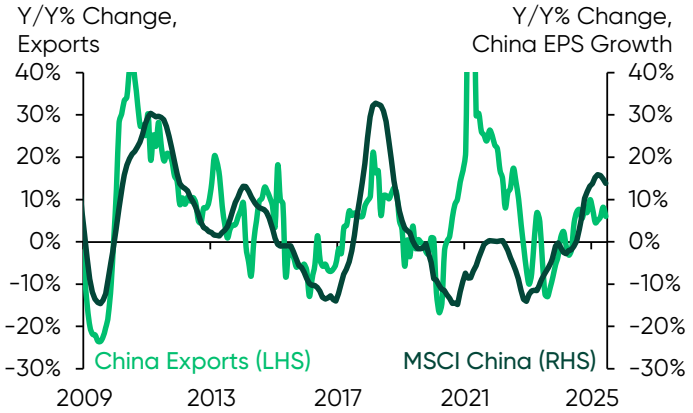
xliv Source: FactSet, as of 07/22/2025. MSCI China, MSCI Emerging Markets and MSCI ACWI with net dividends, in USD, 12/31/2024 – 06/30/2025.

xlv Ibid.

xlvi Ibid.

xlvii Source: Department of Statistics Singapore and Enterprise Singapore, as of 07/22/2025.

EXHIBIT 18: CHINESE EXPORTS SURPRISED TO THE UPSIDE IN 1H25



Source: FactSet, CEIC as of 06/30/2025.

The US is talking of cracking down on transshipping—even including punitive, double tariff rates on goods deemed transshipped in its trade deal with Vietnam. This is a clear shot at China. But there are practical problems. Identifying transshipped goods is exceedingly difficult. In today's globalized world, very few products are made wholly in any one country, including China. If a good is made partly in China and partly in Vietnam, it isn't technically considered transshipped. If made partly in China and partly in Mexico, goods bound for the US could legally enter under much lower tariff rates.

Identifying which goods are and aren't transshipped requires close inspection and monitoring. Yet America's Customs and Border Protection is vastly understaffed, as we wrote last quarter. And, as this quarter's review shows, we are already undershooting estimates of full tariff payments by a wide margin. Policing transshipping looks to be a tall order. It won't surprise us if lingering skepticism toward China's growth proves faulty.

Now, this isn't to say all is well in China. The real estate sector continues faltering and contracting across virtually every metric. Retail sales have cooled of late, growing just 4.8% y/y in June, down from 6.4% in May and 5.1% in April.[xlviii] And, yes, much is made of "deflationary pressures," with broad prices rising just 0.1% y/y in June, the first positive read since January, and so-called factory-gate prices being locked in persist contraction. Furthermore, the government's reverting to infrastructure stimulus and fleeting cash-for-clunkers-like consumer plans fans skepticism over Beijing's ability to avert contraction.

But for markets, all those factors are well-known old news, unlikely to sway returns materially. Furthermore, all the focus on them overlooks the fact total social financing has climbed throughout 2025, boosting money supply. This suggests ample credit is flowing to support consumption and investment. The regulatory uncertainty that drove much of China's weakness in the last four to five years has seemingly abated amid the government's shifting to focus on trade-war mitigation. Lastly, if trade continues to hold up better than expected, all the weak sentiment towards the Middle Kingdom should prove overdone. This is a recipe for the kind of positive surprise that drove the first half's outperformance to last.

xlviii Source: FactSet, as of 07/22/2025.

INDEX DESCRIPTIONS

MSCI ALL COUNTRY WORLD

The MSCI ACWI Index is a free float-adjusted market cap-weighted index that is designed to measure equity market performance of developed and emerging markets. The MSCI ACWI Index consists of 23 developed country and 24 emerging market country indexes. With 2,687 constituents, the index covers approximately 85% of the global investable equity opportunity set. Unless otherwise specified, returns shown include dividends after deducting estimated withholding taxes. MSCI calculates estimated withholding taxes using the maximum rate of the constituent company's country of incorporation applicable to non-resident institutional investors that do not benefit from double-taxation treaties.

MSCI WORLD

The MSCI World Index consists of 23 developed market country indexes. Unless otherwise specified, returns shown include dividends after deducting estimated withholding taxes. MSCI calculates estimated withholding taxes using the maximum rate of the constituent company's country of incorporation applicable to non-resident institutional investors that do not benefit from double-taxation treaties.

MSCI WORLD GROWTH

The MSCI World Growth Index captures large and mid-cap securities exhibiting overall growth style characteristics across 23 Developed Markets (DM) countries. The growth investment style characteristics for index construction are defined using five variables: long-term forward EPS growth rate, short-term forward EPS growth rate, current internal growth rate and long-term historical EPS growth trend and long-term historical sales per share growth trend. Unless otherwise specified, returns shown include dividends after deducting estimated withholding taxes. MSCI calculates estimated withholding taxes using the maximum rate of the constituent company's country of incorporation applicable to non-resident institutional investors that do not benefit from double-taxation treaties.

MSCI WORLD VALUE

The MSCI World Value Index captures large and mid-cap securities exhibiting overall value style characteristics across 23 Developed Markets (DM) countries*. The value investment style characteristics for index construction are defined using three variables: book value to price, 12-month forward earnings to price and dividend yield. Unless otherwise specified, returns shown include dividends after deducting estimated withholding taxes. MSCI calculates estimated withholding taxes using the maximum rate of the constituent company's country of incorporation applicable to non-resident institutional investors that do not benefit from double-taxation treaties.

MSCI EUROPE

The MSCI Europe Index captures large and mid-cap representation across 15 Developed Markets (DM) countries in Europe. With 415 constituents, the index covers approximately 85% of the free float-adjusted market capitalization across the European Developed Markets equity universe. Unless otherwise specified, returns shown include dividends after deducting estimated withholding taxes. MSCI calculates estimated withholding taxes using the maximum rate of the constituent company's country of incorporation applicable to non-resident institutional investors that do not benefit from double-taxation treaties.

Unless otherwise specified, returns shown include dividends after deducting estimated withholding taxes. MSCI calculates estimated withholding taxes using the maximum rate of the constituent company's country of incorporation applicable to non-resident institutional investors that do not benefit from double-taxation treaties. Unless otherwise specified, returns shown include dividends after deducting estimated withholding taxes. MSCI calculates estimated withholding taxes using the maximum rate of the constituent company's country of incorporation applicable to non-resident institutional investors that do not benefit from double-taxation treaties.

S&P 500

The S&P 500 Composite Index is a capitalization-weighted, unmanaged index measuring 500 widely held US common equities of leading companies in leading industries, representative of the broad US equity market. Past performance is no guarantee of future results. A risk of loss is involved with investments in equity markets.

ICE BOFA 7-10 YEAR US CORPORATE

The ICE BofA 7-10 Year US Corporate Index is a subset of the ICE BofA US Corporate Master Index, which tracks the performance of US dollar denominated investment grade rated corporate debt publicly issued in the US domestic market. This subset includes all securities with a remaining term to maturity of greater than or equal to 7 years and less than 10 years. When the last calendar day of the month takes place on the weekend, weekend observations will occur as a result of month ending accrued interest adjustments.

NASDAQ COMPOSITE

The Nasdaq Composite Index is a market capitalization-weighted index of more than 2,500 equities listed on the Nasdaq stock exchange. It is a broad index that is heavily weighted toward the technology sector. The index is composed of both domestic and international companies.

MSCI EMERGING MARKETS

MSCI Emerging Markets Index is a free float-adjusted market cap-weighted index that is designed to measure equity market performance of emerging markets. The MSCI Emerging Markets Index consists of 24 emerging market country indices. Unless otherwise specified, returns shown include dividends after deducting estimated withholding taxes. MSCI calculates estimated withholding taxes using the maximum rate of the constituent company's country of incorporation applicable to non-resident institutional investors that do not benefit from double-taxation treaties.

MSCI EAFE

The MSCI EAFE Index is designed to represent the performance of large and mid-cap securities across 21 developed markets, including countries in Europe, Australasia and the Far East, excluding the U.S. and Canada. The Index is available for a number of regions, market segments/sizes and covers approximately 85% of the free float-adjusted market capitalization in each of the 21 countries.

Should you have any questions about any of the information in the Second Quarter 2025 Review and Outlook, please contact us at +1 (800) 851-8845 or FisherInstitutional@fi.com.

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