STOCK MARKET OUTLOOK

2025: Part III

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2025 STOCK MARKET OUTLOOK – PART III

July 22, 2025
Executive Summary

Global stocks proved a timeless truth about corrections (sudden, steep, sentiment-driven -10% to -20% declines) 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, -9.3% slide after April 2's tariff shock.[1] Yet the round trip netted out to an 11.5% MSCI World Index quarterly rise, reminding the world how quickly markets move on after pricing in even real negatives.[2]

Stocks' downswing was an archetypal correction, classic in every way. It was a short, sharp shock featuring a huge scary story: tariffs. 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 stocks 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 much lower-than-expected tariff revenues eased fears of the economic effects. Even the conflict in the Middle East barely interrupted markets' fast recovery.

While the fact we have already had a correction this year doesn't preclude having another one or experiencing more volatility, Q2's rally seems like a down payment on strong full-year returns. We remain bullish, and our forecast is intact. Stocks have already exceeded 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 stocks are leading, though US and growth stocks are doing fine. Politics remain 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 concerns, but we think all are discussed too widely to have much effect on stocks.

Bond markets' behavior was also emblematic of a correction, especially in corporate bonds, where yield premiums over Treasurys widened substantially amid stock market volatility, then reverted to historically low levels—a reminder that bonds aren't immune to short-term sentiment swings. As with stocks, there was a scary story 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 pearl clutching. But 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 stock or bond markets. The debate is too noisy and public, the associated forecasts scrutinized to death. 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 fall further as budget debates wind down overseas.

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Meanwhile, to no fanfare, the global yield curve has steepened—especially outside America, supporting non-US leadership. 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, as sensible as the argument may be, the more it incentivizes Fed head Jerome Powell to wait. His primary job at this juncture, alas, 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 abroad.

While it is rare for stocks to suffer more than one correction in a year, further volatility is always possible. Lingering tariff uncertainty is a wildcard. The July 9 expiration of Trump's 90-day reciprocal tariff pause is one source of such uncertainty. But there are others, including the status of deals, pending appellate court reviews of challenges to Trump's main tariffs and others.

But regardless of short-term wiggles, we think this bull market has significant room to run. Headline fears are part of the wall of worry this bull market should climb. New highs after a correction tend to breed new highs, not fresh declines. If you need long-term growth to reach your goals, you need to be invested in up markets. Enduring volatility and corrections won't prevent you from reaping stocks' long-term returns. Missing bull markets will.

Here is a quick preview of this Stock Market Outlook's appendixes:

- Appendix I recaps market movement, our forecast, global leadership trends by country and revisits the various tariff scenarios we laid out last quarter. Additionally, it looks at several ancillary fears that cropped up during the first half.
- In Appendix II, we look closer at drivers favoring European and non-US stocks—as well as value stocks—looking forward.
- The OBBBA was on many investors' minds after becoming law on July 4. Appendix III gives a recap of what is in it, why we think it isn't likely to sway markets much and why forecasts of debt doom stemming from it are well wide of the mark.

Table of Contents

Appendix I: The Correction and Beyond **4**
Forecast Recap 5
The Tariff Scenarios 8
Scenario 1: Tariffs Prove Illegal and Unenforceable 8
Scenario 2: Dealmaking Galore 9
Scenario 3: Coordinated Retaliation 9
New Scenario 4: Non-US Actions Free Global Trade Further 10
What About Manufacturing Returning to America? 10
Regional Conflict Didn't Sink Stocks 10
The 'Weak' Dollar 11
Zoom Out on Rates, Too 11
Appendix II: Factors Fueling Non-US Leadership **13**
The Steepening Global Yield Curve 13
The Eurozone's Engine Is Revving Up 15
Bullish Britain Isn't Brittle 16
Japan Returns to Normal 17
Appendix III: On the Big Beautiful Bill **19**
Key Provisions in the OBBBA 19
OBBBA Debt Perceptions Don't Match Reality 19
Spread Out Over 10 Years, Debt Projections Are Relatively Modest 20
Besides, Anything Can Happen in 10 Years 20
Inflation Further Mitigates Any Impact 21
Debt Isn't Inherently Negative for Stocks 22

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Appendix I: The Correction and Beyond

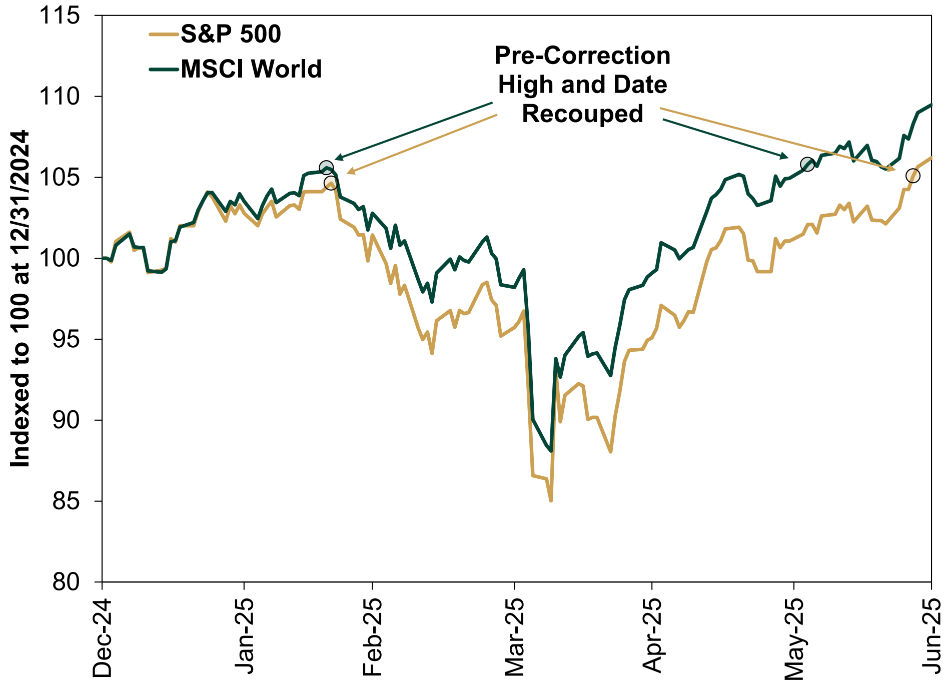
Amid the depths of the first half's correction (sharp, sentiment-driven, -10% to -20% drop) in April, few could envision 2025 turning out to be a good year. Blinded by volatility, most could only see more downside ahead in what they were sure was a bear market driven by tariffs.

But we remained bullish. For one, we laid out several scenarios in our Q2 Stock Market Outlook, noting the likeliest outcome was tariffs' effects proving 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 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 stock prices. Once they did, a lightning-fast rebound followed, with world stocks roundtripping to new all-time highs by June 3 and US stocks getting there June 26.

Exhibit 1: The First Half's Correction and Recovery



Source: FactSet, as of 7/7/2025. S&P 500 Total Return and MSCI World Index with net dividends, 12/31/2024 – 6/30/2025.

Many sweat the quick recovery as "too far, too fast"—a normal post-correction sentiment, but one that feeds many behavioral investment errors. It can make you avoid stocks for backward-looking reasons and miss gains that compound later. There is nothing atypical about last quarter's swift slide and rapid recovery. Exhibit 2 demonstrates this, showing Q1's downturn and recovery closely resemble the median correction and recovery.

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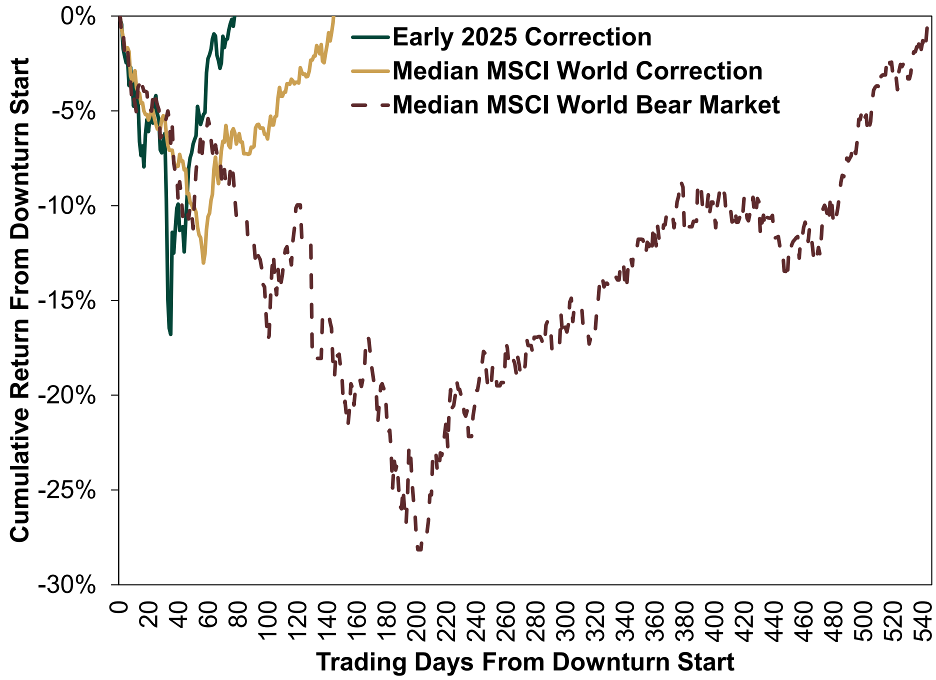
Some see a correction as a sign of a shaky bull market, but we think this is backward. Corrections' sting and lingering fear help reset expectations lower. This takes potential ebullience off a bull market, helping facilitate the positive surprise that fuels rising stocks. A strong bull market *needs* some skepticism or pessimism. Corrections help foster it. This is why history's longest bull market, in 2009 – 2020, featured eight.[3]

Exhibit 2: The Correction's Rapid Rebound



Source: FactSet, as of 7/11/2025. MSCI World Price Index, 2/18/2025 – 6/6/2025 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 *despite* the correction.[4] 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.

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

While many see tariffs as a policy that protects, encourages or fosters domestic industry over imports, this is rarely true. Tariffs hit the *imposing* nation harder than targeted countries. They can sway prices. They can interfere with businesses' plans. And they discourage investment.

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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.

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%.[5] Mexico? It rose 30.9% in the first half.[6] Even China—the major target of tariffs—rose 17.3%, easily eclipsing US stocks.[7] We expect this non-US leadership to persist, fueled by tariffs' effects, dour sentiment toward non-US stocks and the steepening global yield curve—a fundamental positive for the value firms that dominate Europe. (Appendix II details these factors more.)

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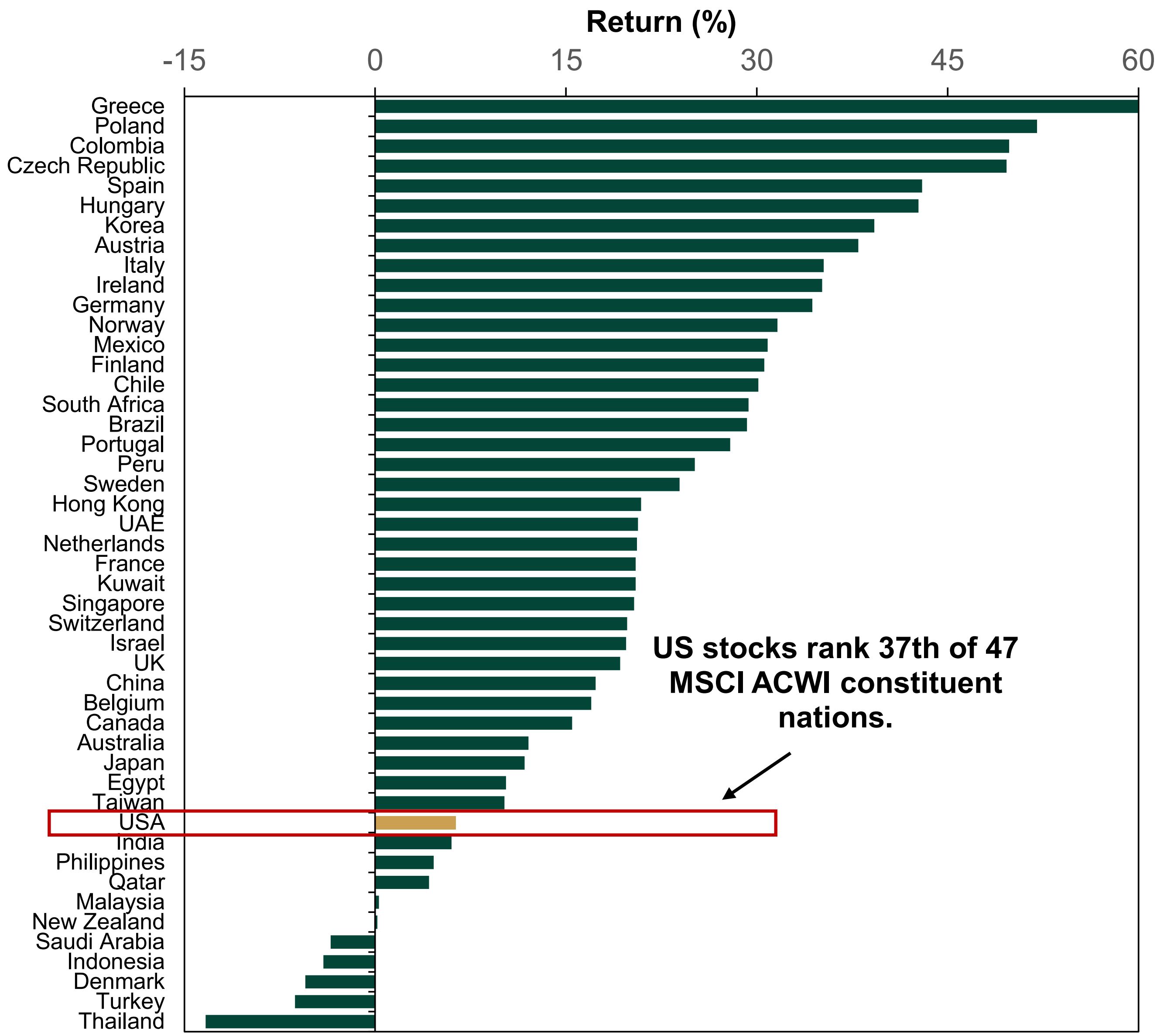
Exhibit 3: First Half Returns by Country



Source: FactSet, as of 7/16/2025.

Value outperformed alongside Europe and non-US stocks. 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 US growth and Tech stocks 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 stocks appear poised for a good year, with the correction having reset sentiment much lower everywhere.

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Political uncertainty has already eased from the year's start and its peak in April, especially with Trump's signature budget bill passing in early July. (Appendix III) 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.[8] M2, while accelerating after very slow growth in 2024 (and contraction before that), is far off February 2021's peak rate above 25% y/y.[9] At 4.5% y/y in May, it too matches pre-COVID trends. Yes, many still see tariffs as a threat. But the little data we have post-implementation don'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' hamstringing 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 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. Let us explain.

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 help 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.[10] Hence, year to date, the $91 billion in cumulatively collected tariffs is a fairly significant rise.[11] But it pales next to the $229 billion worst-case scenario estimate based on the face value of tariffed imports.[12]

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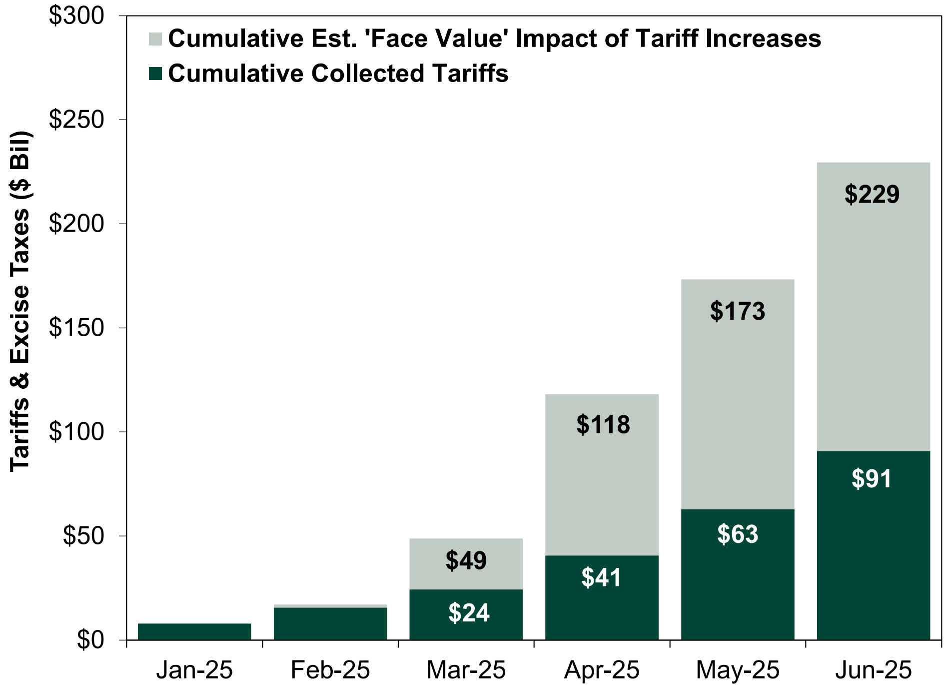
Exhibit 4: Tariff Collection YTD Versus Worst Case



Source: Customs and Border Protection, Fisher Investments Research, as of 7/3/2025.

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: with 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.

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.

Scenario 3: Coordinated Retaliation

Status: Few Signs This Is Happening

In April, we couldn't dismiss retaliation. China had already 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 recently: Non-US nations banding 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. Others 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 do we incorporate that into our outlook?

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, stocks care little about *where* something is made. They care about profits and revenue. Making investment decisions based on a manufacturing revival risks being premature at best and wrong at worst.

Regional Conflict Didn't Sink Stocks

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, stocks barely blinked and oil prices retreated quickly. By June 24's ceasefire, global *and Israeli* stocks exceeded pre-conflict levels. Brent crude oil—the global benchmark—was below it. This is the latest example illustrating regional war rarely moves markets materially.

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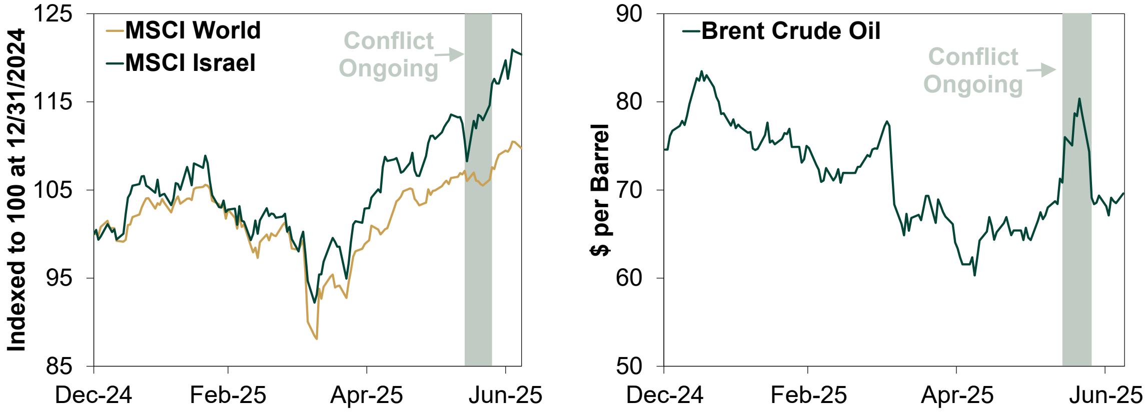
Exhibit 5: The 12-Day War Barely Sways Stocks and Oil



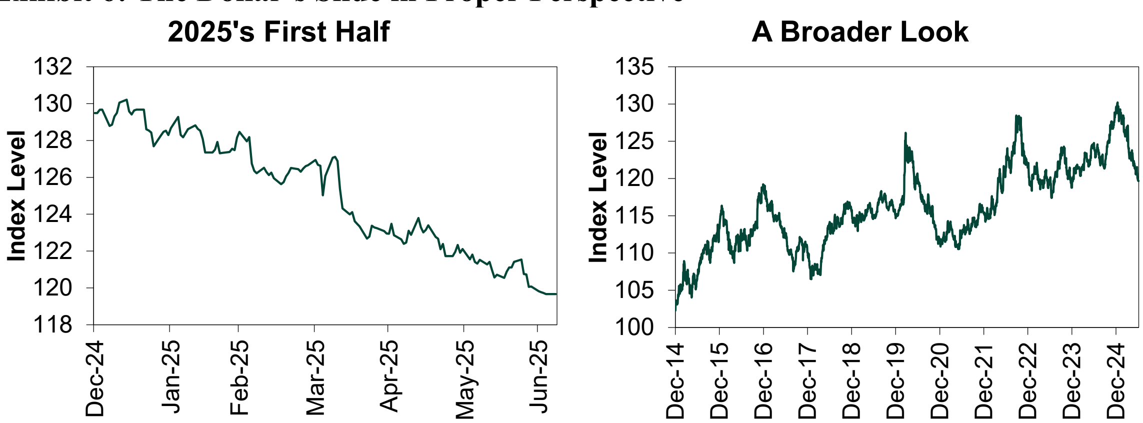
Source: FactSet, as of 7/8/2025. MSCI World and MSCI Israel with net dividends, Brent crude oil, 12/31/2024 – 7/7/2025.

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, zoom out. 2025's slide merely reverses late 2024's surge, putting the dollar at levels many deemed too strong for years.

Currencies always trade in pairs and, in the long run, major ones simply waffle, 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 7/8/2025. Trade-Weighted US Dollar Index (Broad), 12/31/2014 – 7/7/2025.

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. (Appendix III) 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.[13] UK yields fell -18 basis points.[14] Japan's yields similarly fell -8 basis points.[15] Canadian yields rose, but only 24 basis points.[16] 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 in Q2

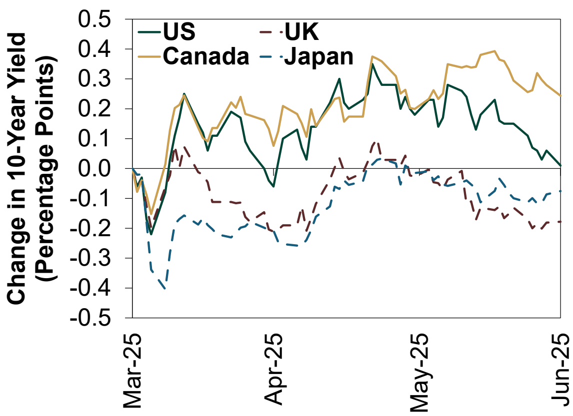
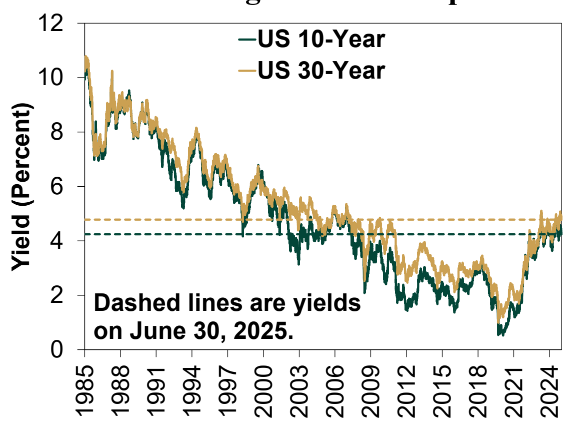


Exhibit 8: US Long Rates in Perspective



Source: FactSet, as of 7/14/2025.

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Appendix II: Factors Fueling Non-US Leadership

Non-US stocks led again in Q2 and remain far ahead of US stocks year to date, up 19.0% versus the S&P 500's 6.2%.[17] While US markets recouped some ground since late April, this is likely a byproduct of US stocks 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 stocks—Europe's bread and butter—are stealthily improving. Chief among them: the steepening yield curve.

The Steepening Global Yield Curve

The yield curve plots interest rates from short (typically 3-month) to long (10-year). It is "steep" when long rates top short, the curve sloping upward. It is "inverted" when short rates top long rates, sloping downward. For over a century, steep curves generally predicted growth, while inverted curves often (but not perfectly) predicted recession.

When the yield curve inverted in late 2022, nearly every professional noticed. Stocks 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. When the US and global economies kept growing—and stocks rallied despite inversion lasting through 2024—everyone moved on. Now, with no one looking, it is steepening.

The inverted yield curve is like a flashing "check engine" light on your car's dash. It usually means trouble. But it could be a misfire. To know, you must pop the hood and dig in. 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.

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 dirt-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.[18] 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.

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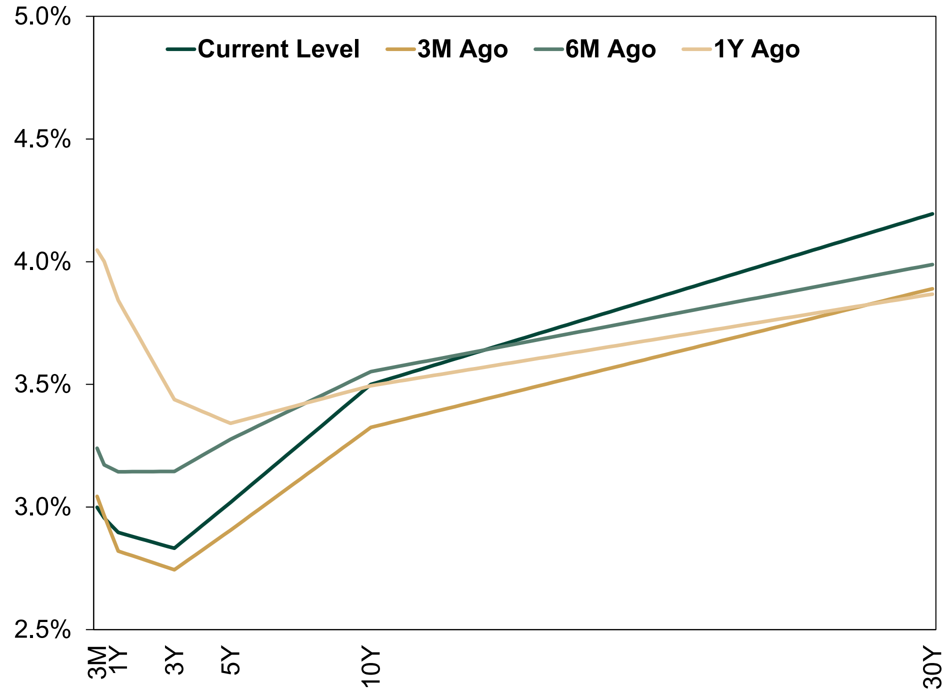
While most traditionally focused on the US curve, we have long used a global curve, weighting regions according to their share of developed-world GDP. As Exhibit 9 shows, its spread jumped from -0.55 percentage point (ppt) inversion a year ago to 0.50 ppt, a swing of over 1 ppt. Most of this comes from Europe and Asia, while the US's curve—though improved—remains flattish. (Exhibit 10) Tailwinds are stronger abroad.

Exhibit 9: The Steepening Global Yield Curve



Source: FactSet, as of 7/7/2025.

Exhibit 10: 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 7/7/2025.

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

While growth stocks abound in the US, value dominates Europe. As Exhibit 11 shows, Europe's top four sectors—over half of its market cap—are value-heavy. The top two, Financials and Industrials, are utterly trouncing global returns, up 38.7% and 39.2%, respectively.[19] No shock here, considering steeper curves directly boost bank profits and funnel piles of cash to value-rich Industrials.

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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. Discretionary—heavy with growth-oriented e-commerce—also has a large weighting, while America's Financials sector pales in comparison to Europe's.

Exhibit 11: Europe's Value Tilt

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 7/16/2025. S&P 500 and MSCI Europe Index sector weights on 6/30/2025.

The Eurozone's Engine Is Revving Up

Calling eurozone sentiment dim is 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 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 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 French 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 12) The inflation war is over, rendering high rates unnecessary.

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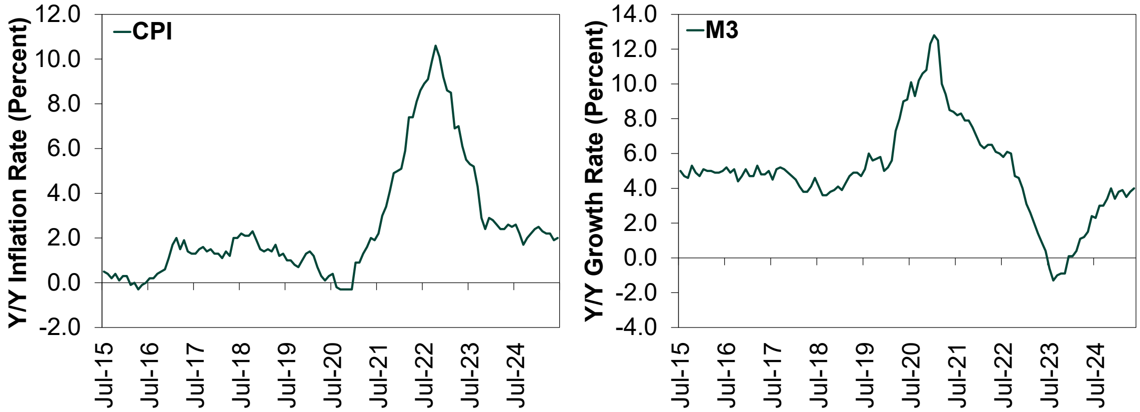
Exhibit 12: Eurozone Inflation and Money Supply



Source: FactSet, as of 7/10/2025. 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 processes are increasingly normal there, as are fractious coalitions featuring populist parties. Yet Dutch stocks are up 20.6% year to date, more than doubling global returns.[20]

Bullish Britain Isn't Brittle

The UK also has a big wall of worry, with shaky economic data fueling pessimism despite UK stocks' 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 tax hikes don't appear to be harming growth as widely feared. Moreover, 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 this month. 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 13) 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.

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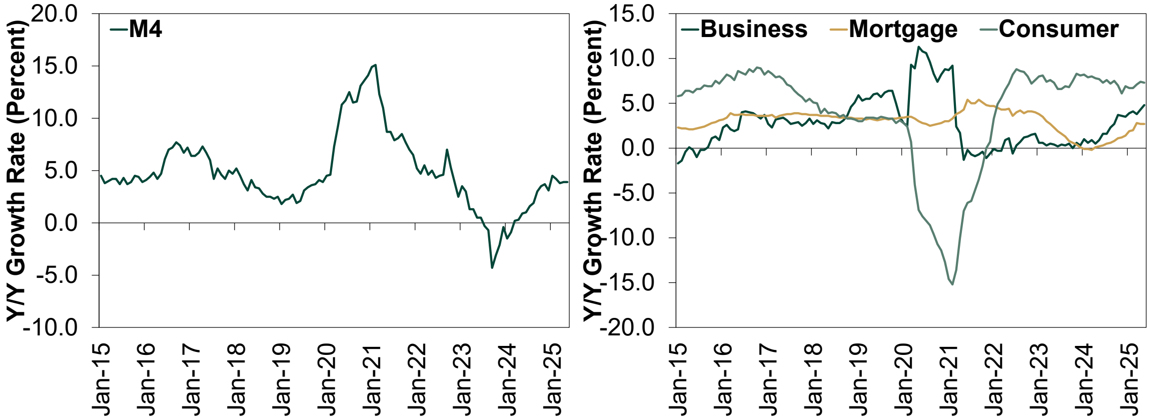
Exhibit 13: UK Money Supply and Lending



Source: Bank of England, as of 7/10/2025. 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's welfare reforms flopped in July, passing in watered-down fashion, analysts speculated about more tax hikes and Reeves's future. A potential wealth tax is the latest scare, and pundits hype every rumor of Reeves's downfall.

Yet as in France, UK public finances are a political issue more than an economic one. As inflation boosted tax revenues, interest costs became even more affordable—a point no one mentions. (Appendix III has more on this concept in America.) Deficit concerns stem not from reality but from rules requiring borrowing to fit in a narrow box dictated by the nonpartisan watchdog's economic forecasts. This keeps fiscal policy on shifting sand, forcing governments to tweak taxation and spending as forecasts evolve. There is a growing awareness in UK political ranks that this injects uncertainty, discouraging risk-taking and forcing both political parties to increase the country's tax burden. 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.

The upshot is gridlock. The welfare rebellion diminished Starmer's political capital, while the upstart Reform party's continued polling ascent puts his Labour Party on notice. Both create incentives not to rock the boat with big legislation, a bullish factor.

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 March 2024, Japan's yield curve spread widened by 30 basis points. Long rates rose more than short—a return to normal. Banks now have more latitude to fund economic growth.

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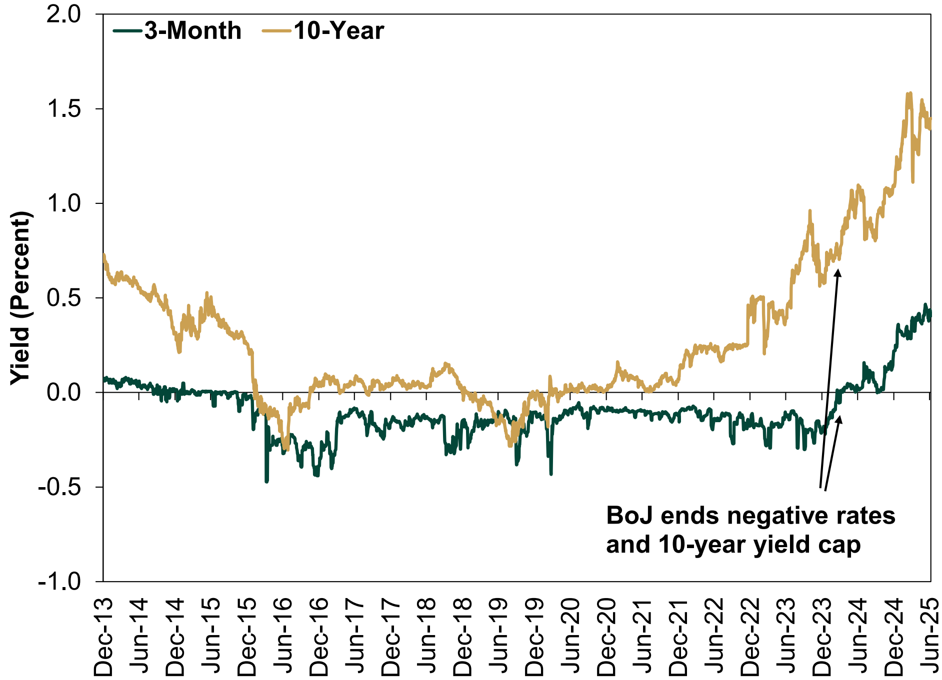
Exhibit 14: Japan's Return to Monetary Sanity



Source: FactSet, as of 7/8/2025. Japanese 3-month and 10-year bond yields, 12/31/2013 – 7/7/2025.

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.[21] Household consumption grew 0.5% annualized, while business investment jumped 4.4%.[22] 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 pothole 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.

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Appendix III: 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) on 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 raises 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 stocks, 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 nothingburger 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 sweat 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.

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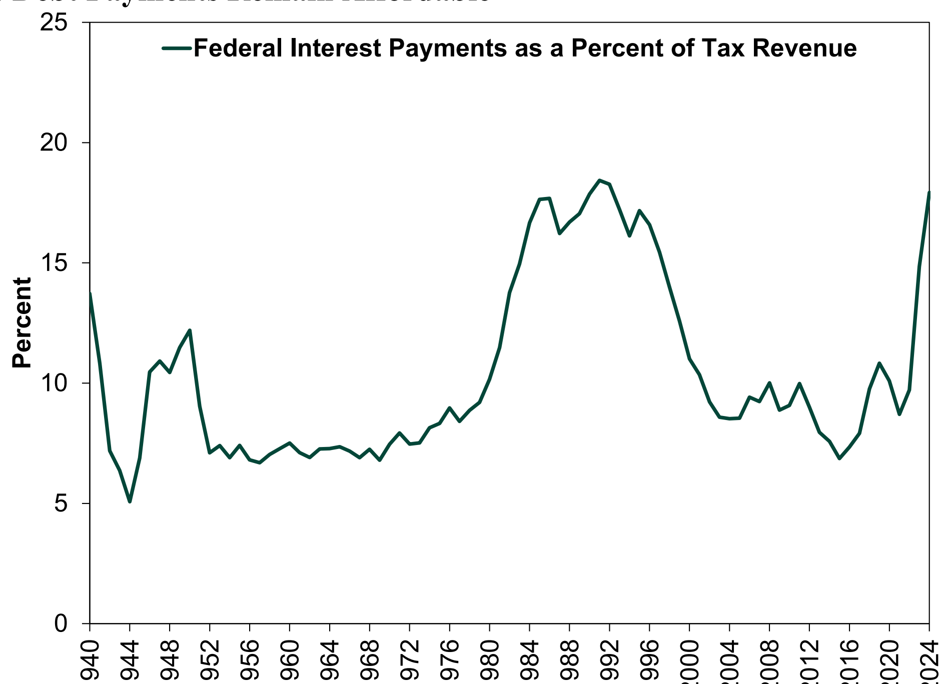
Spread Out Over 10 Years, Debt Projections Are Relatively Modest

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.[23]

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%.[24] Whatever your view of the borrowing binge, there is little to suggest markets couldn't digest 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 15: Debt Payments Remain Affordable



Source: Federal Reserve Bank of St. Louis, as of 7/7/2025.

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 Cuts 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.[25] But, years later, the CBO reported: "Nominal

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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."[26] (Boldface ours.)

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 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 gospel. Which markets know—likely why bond yields didn't react materially to the OBBBA's passage. Trust them.

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 grand for Uncle Sam, 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%.[27] 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.[28]

Not only does inflation mitigate repayment in real terms, it also boosts revenue. Nominal US GDP is $30 trillion.[29] 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.[30] This would dwarf the CBO's 1.4% – 1.8% (around $400 – $550 billion) annual projected debt increase from the OBBBA.

Notice what this entails. Given Uncle Sam's tax take stays about the same percentage-wise—which the OBBBA enshrines—in addition to the $780 billion inflation shrink, tax revenue rose some $250 billion.[31] Subtract those, and 2024's $1.9 trillion of added debt falls even further to $870 billion. More than half the supposedly gargantuan flow of red ink is thus vaporized!

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 Stocks

Third, debt isn't inherently negative for the economy or markets. Some amount of debt—or credit—is essential for capitalist production, an unalloyed positive. Owing more than you can afford is, of course, never great. But used wisely, debt can be productive. It helps companies expand. It helps people finance a home. And it helps countries invest more than they would otherwise. Just as issuers can take on too much debt, they can also employ too little.

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—that is standard corporate finance. 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%.[32] 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.[33] America's total assets: $314 trillion.[34] America's return on assets, therefore, yields approximately 9.4%—nearly three times its borrowing cost.

To be crystal 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 stocks. 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.

We hope you have found this information helpful. Please contact Fisher Investments at 800-568-5082 for more information on our outlook and services, or to arrange an appointment with one of our representatives for a complimentary review of your portfolio. To follow our ongoing commentary on market and economic events, please visit our *MarketMinder* blog on Fisher Investments' corporate website: https://www.fisherinvestments.com/en-us/marketminder. Alternatively, you can sign up here for *MarketMinder's* weekly newsletter.

The Investment Policy Committee
Aaron Anderson, Ken Fisher, Bill Glaser, Michael Hanson and Jeff Silk

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[1] Source: FactSet, as of 7/2/2025. MSCI World Index return with net dividends, 4/2/2025 – 4/4/2025.
[2] Ibid. MSCI World Index return with net dividends, 3/31/2025 – 6/30/2025.
[3] Source: FactSet, as of 7/7/2025. Count based on MSCI World corrections, 3/9/2009 – 2/12/2020.
[4] Source: FactSet, as of 7/8/2025. S&P 500 total return, 12/31/2024 – 6/30/2025.
[5] Source: FactSet, as of 7/16/2025. MSCI Canada return with net dividends and MSCI USA return with gross dividends, 12/31/2024 – 6/30/2025.
[6] Ibid. MSCI Mexico return with net dividends, 12/31/2024 – 6/30/2025.
[7] Ibid. MSCI China return with net dividends, 12/31/2024 – 6/30/2025.
[8] Source: Center for Financial Stability, as of 7/8/2025.
[9] Source: Federal Reserve Bank of St. Louis, as of 7/7/2025.
[10] Source: Statistics Singapore, as of 6/15/2025.
[11] Source: US Customs and Border Protection, as of 7/3/2025.
[12] Source: Fisher Investments Research, as of 7/3/2025.
[13] Source: FactSet, as of 7/8/2025. US 10-Year Treasury yield change, 3/31/2025 – 6/30/2025.
[14] Ibid. UK 10-Year Gilt yield change, 3/31/2025 – 6/30/2025.
[15] Ibid. Japan 10-Year JGB yield change, 3/31/2025 – 6/30/2025.
[16] Ibid. Canada 10-Year Government Bond yield change, 3/31/2025 – 6/30/2025.
[17] Source: FactSet, as of 7/7/2025.
[18] Source: US Federal Reserve, as of 5/14/2025. Assets and Liabilities of Commercial Banks.
[19] Source: FactSet, as of 7/7/2025. MSCI Europe Industrials and MSCI Europe Financials returns with net dividends, 12/31/2024 – 6/30/2025.
[20] Ibid. MSCI Netherlands return with net dividends, 12/31/2024 – 6/30/2025.
[21] Source: FactSet, as of 7/8/2025.
[22] Ibid.
[23] Source: FactSet, as of 7/7/2025.
[24] Source: FactSet, as of 7/7/2025.
[25] "The Budget and Economic Outlook: 2018 to 2028," Staff, CBO, April 2018.
[26] "Additional Information About the Effects of Expiring Provisions of the 2017 Tax Act in CBO's Baseline Projections," Phill Swagel, CBO, 12/4/2024.
[27] Source: US Bureau of Labor Statistics, as of 6/11/2025.
[28] Ibid.
[29] Source: US Bureau of Economic Analysis, as of 6/26/2025.
[30] Source: Federal Reserve Bank of St. Louis, as of 7/7/2025.
[31] "How I Learned to Stop Worrying About the National Debt – Even Though It's $35 Trillion," Ken Fisher, *New York Post*, 11/25/2024.
[32] Source: US Treasury, as of 6/30/2025.
[33] Source: US Bureau of Economic Analysis, as of 6/26/2025.
[34] Source: Federal Reserve and S&P Global, as of Q4 2024.

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