

Doll's Deliberations®

Weekly Investment Commentary



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Summary

Equities rose again last week (S&P 500 0.99%) with the S&P and NASDAQ finishing just below record highs. Small stocks recorded another strong week. The White House announced another 90-day extension of China's tariff deadline. Best sectors for the week were healthcare (4.65%), consumer discretionary (2.53%), and communication services (2.13%); worst sectors were consumer staples (-0.68%), utilities (-0.66%), and industrials (-0.19%).

Key takeaways

1. CPI headline inflation held steady at 2.7% while the core rate rose to 3.1%. The probability of a September 25-basis-point (bp) rate cut is over 90%. (A 50-bp cut is less than a 10% probability.)
2. Market expectations remain for two 25-bp cuts this year and three 25-bp cuts next year. (The equity market rally makes us think that a lot of good news is already accounted for.)
3. The Atlanta Fed's "GDP Now" forecaster is predicting a 3.7% second-quarter GDP DECLINE.
4. If there were no further changes to tariff rates, we assume that the average effective tariff rate on imported goods would peak out at 14.4%. (This compares to an average effective tariff rate in 2024 of 2.4%.)
5. The biggest complaint we often hear is how prices are higher today than they were in the past. (It is not the growth rate that is a concern, but that the level today takes a larger share of the wallet.)
6. 2Q earnings were exceptionally good. 90% of the S&P 500 has reported 2Q earnings. More than 75% of companies have exceeded earnings expectations, same for revenues. More than 60% have had double beats.
7. For now, companies are eating the tariffs, with limited pass-through to the consumer. (That helps explain why hiring is weak. Companies are trying to protect margins.)
8. Technology companies account for a third of S&P 500 earnings, three times its share of 20 years ago. (Technology sourced nearly three-quarters of 2024 earnings growth.)
9. The S&P 500 index has risen by 8% YTD and is near an all-time high, but dispersion within the equity market has been high. The median stock remains 12% below its 52-week high.
10. The top 10 stocks make up approximately 40% of the S&P 500. Strategas: "The S&P 500 is no longer a truly diversified investment; at this point, it resembles a concentrated portfolio."

Equity markets (Index total return %)	Last week	Year-to-date
DJIA	1.79	6.72
S&P 500	0.99	10.55
NASDAQ	0.83	12.42
Russell 1000	1.26	10.61
Russell 1000 Growth	0.68	12.22
Russell 1000 Value	1.38	8.20
Russell 2000	3.66	3.93

S&P equity sectors (Index total return %)	Last week	Year-to-date
Communication services	2.13	18.11
Consumer discretionary	2.53	1.26
Consumer staples	-0.68	6.98
Energy	0.78	1.73
Financials	1.18	9.38
Healthcare	4.65	-0.09
Industrials	-0.19	14.92
Information technology	-0.12	15.93
Materials	1.85	9.24
Real estate	0.20	3.23
Utilities	-0.66	14.69

Markets are priced for declining inflation (we're skeptical)

The enthusiasm of investors is becoming increasingly (and perhaps excessively) evident. Each new event is being interpreted more positively than would be warranted had global liquidity conditions not been so increasingly buoyant. The latest peculiar interpretation of new data was last week's U.S. CPI report, which was widely seen as benign and consistent with imminent Fed easing. This spin ignored the fact that the report again confirmed that underlying inflation has flattened well above the Fed's 2% target and, in fact, may even be edging higher.

Meanwhile, fatigue with the constant flip-flopping of U.S. tariff policy means that new threats have progressively had less impact on investor sentiment. This is despite the fact that while the tariff endpoint is still unclear, it will most certainly be with the highest rates since the Great Depression. The U.S. and global economy are seen as being resilient enough to weather the drag from high tariffs. And U.S. inflation is seen as being, at worst, only mildly and temporarily impacted by tariffs.

The result of these spins/biases is that there is now a strong consensus that the Fed will resume cutting its policy rate next month, with a significant lowering of the rate now expected over the next year. The administration continues to aggressively pressure the Fed to take such action, regardless of the inflation data. We generally agree with the view of economic resilience (although we think the risk is for more weakness) but disagree on the inflation outlook, especially for the U.S., and thus do not expect a waterfall decline in U.S. rates and bond yields. Corporate profits and household finances remain strong. This, plus looming fiscal stimulus in the U.S. and euro area and ongoing accommodative monetary conditions, should more than offset the economic impact from higher U.S. tariffs.

Inflation and policy risks are being downplayed, which supports ongoing risk-taking. We remain on guard for an upsetting of the applecart from policymakers and investors eventually realizing that inflation is hotter than appreciated, causing bond yields to rise and P/Es to fall. For now, the inflation and policy risks are being downplayed, which is positive for risk asset markets. To us, investors are downplaying stretched risk-asset valuations, signs of speculative excesses, and the threat that inflation will not return to 2% or less absent a recession. Fiscal excesses will be ignored until the bond market riots.

Adding it up, ongoing supportive liquidity conditions and relatively calm bond markets mean additional asset-price inflation. This process should continue until investors realize they have been too optimistic on a return to 2% inflation.

Conclusion

U.S. inflation data are not benign, and there is the possibility that CPI will sequentially firm over the balance of the year, leaving the rate well above the Fed's 2% target. Nevertheless, the Fed is primed to resume easing next month, which may keep bond bulls complacent and stocks continuing to overheat.

International equity markets (Index total return %)	Last week	Year-to-date
MSCI ACWI	1.24	14.28
MSCI ACWI EX U.S.	1.38	21.57
MSCI EAFE	1.49	22.48
MSCI EM	1.51	20.37

Fixed income markets (Index total return %)	Last week	Year-to-date
Bloomberg U.S. Aggregate Bond	0.14	4.54
Bloomberg U.S. Corp High Yield	0.26	5.58
Bloomberg U.S. Gov/Credit	0.13	4.46
Bloomberg U.S. T-Bill 1-3 Month	0.05	2.68

Alternatives (Index total return %)	Last week	Year-to-date
Real estate (FTSE NAREIT)	0.16	0.91
Commodities (DJ)	-0.33	4.40
Global listed private equity (Red Rocks)	1.32	10.84
Currencies (DB Currency Future Harvest)	0.34	-0.65

Source: Bloomberg as of Aug. 15, 2025

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