

# Market View July

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## Executive Summary

- The military conflict between Israel and Iran had limited market impact. Investor focus has shifted back to US tariff decisions and the budget reconciliation bill, known as the One Big Beautiful Bill.
- The S&P 500 reached new highs, driven by mega-cap technology stocks. Historical patterns suggest continued gains over the coming months.
- The German fiscal package is expected to take full effect in 2026, when the government will likely take on around EUR 200 billion in new debt – a stimulus that could boost GDP growth to around 2%.
- A Goldilocks scenario is forming, characterized by moderate growth, easing inflation and supportive financial conditions.
- Over the next 6 to 12 months, market liquidity is set to improve significantly as the Fed is expected to start cutting interest rates in the fall and financial deregulation frees up capital at banks.
- Tariff reintroduction, political brinkmanship and liquidity constraints related to the Treasury General Account (TGA) may introduce short-term volatility.
- We prefer so-called debasement trades (equities, gold, bitcoin), are cautious about the USD and bullish on emerging markets.
- In a portfolio context, we believe that it is important to diversify with alternative assets as long-duration bonds may lose their defensive properties if fiscal excesses persist.

## Monthly Review

The short-lived nature of political events proved true in June. While the military escalation between Israel and Iran dominated the news during the month, its impact on the stock market was limited. Crude oil prices quickly stabilized and returned to previous levels. The same held true for gold. Overall, the equity market showed only a moderate response. Investors are now turning their attention to the upcoming tariff deadline on 9 July and the comprehensive US legislative package known as the One Big Beautiful Bill.

## Market Development

### WORLD

The S&P 500 returned to all-time highs, led by a sharp resurgence in mega-cap tech. Four of the Mag-7 stocks outperformed the index in June, confirming Big Tech's return to leadership. The S&P 500 rally mirrored historical V-shaped recoveries. According to SubuTrade, such sharp rebounds tended to be followed by strong subsequent returns. Over the following 3 months the performance was always positive, with a median gain of +6.8%.

### EUROPE

Germany is ramping up fiscal stimulus with net new government borrowing projected to reach over EUR 200 billion annually, or around 4% of GDP, from 2026 onward. The increase is driven by infrastructure and defense spending. The growth impact of the fiscal expansion is likely to peak in 2026, when real GDP growth is projected to reach 2%, according to Deutsche Bank. In comparison, the German economy slightly contracted in 2024 and is expected to grow by 0.5% this year. Without structural reforms, however, the deficit-financed growth impulse will diminish after 2026.

### SWITZERLAND

As cryptocurrencies grow in popularity, central banks are actively exploring Central Bank Digital Currencies (CBDCs) and their integration into existing systems. The Swiss National Bank (SNB) will extend its Project Helvetia pilot program for CBDCs until at least mid-2027. Since late 2023, the SNB has been testing CBDCs for the settlement of tokenized assets via the SIX Digital Exchange.

## Goldilocks revisited?

With geopolitical risks easing, tariff fears diminishing and interest rate cuts by the US Federal Reserve (Fed) expected to begin in the fall, a Goldilocks scenario increasingly comes to mind. We think that under-allocated investors are feeling more pressure to chase the US stock market rally.

Meanwhile, Washington has re-established itself as a less isolationist actor on the global stage with its military response in Iran and active role at the NATO summit. Fears of oil supply disruptions have eased, crude prices have come down and inflation data has remained surprisingly soft – conditions that support rate cuts in the second half of this year and a shift back to secular growth narratives like artificial intelligence (AI).

We expect meaningful easing of market liquidity over the next 6 to 12 months. Global disinflationary surprises in recent months have prompted most central banks to declare victory on inflation, with the Fed being the notable exception so far. While Fed Chairman Powell delivered a once-in-a-generation soft landing and acted prudently in keeping monetary policy stable during the second quarter, his influence may wane after the annual Jackson Hole meeting in August. A Trump-aligned, more dovish successor could be nominated by fall, setting the stage for a policy pivot into 2026. We may see a shift from moderately dovish to aggressively dovish policy – especially if institutional independence is challenged. In addition, financial market deregulation is advancing as the Fed recently published a proposal to relax bank capital requirements. Steno Research estimates that the reform could free up to USD 150-200 billion in lending capacity, acting as a powerful procyclical force.

The productivity boom led by AI could begin to materialize. AI has been the sole narrative that has not faded in past years. Hyperscalers have already spent approximately USD 477 billion on capex (2022-2024), with projections of USD 1.15 trillion through 2027, according to Goldman Sachs. We believe these investments may soon show up in corporate results, shifting sentiment from thematic excitement to tangible earnings growth. Despite these positive developments, many market participants remain focused on downside risks, in particular on tariffs. The trajectory of Trump's trade policy may hinge on the passing of his One Big Beautiful Bill (OBBB) before the expiration of the 90-day tariff pause on 9 July. As of writing, the tax and spending bill was passed by the Senate and still needs approval by the House of Representatives. If the bill is passed quickly, Trump may resume a more aggressive trade stance. Yet with approval ratings under pressure and the 2026 midterm elections approaching, we expect another extension or some kind of exit scenario in the form of "fake" deals. Trump's recent approach to trade – nicknamed "TACO" by critics (short for Trump Always Chickens Out) – suggests a reluctance to provoke another period of market instability or recession fears. This interpretation is supported by the removal of the contentious Section 899 from the OBBB, a clearly positive development. For additional context regarding Section 899, please see our June Market View.

## Positioning

We believe that the market consensus still underestimates the potential for significant upside. Economic growth could come in stronger than expected in the second half of 2025 and 2026, largely because of further easing in monetary policy and financial deregulation in the US. In addition, the OBBB aims to boost growth, just as German fiscal stimulus does. On a micro-level, the adoption of artificial intelligence should lead to productivity gains, which should soon be visible in corporate earnings. In the short term, the weaker US dollar is supportive for internationally active US companies.

Of course, risks remain. The possible reintroduction of tariffs, a slower U-shaped economic trajectory and continued political brinkmanship in the US could inject volatility. The Q2 earnings season, which will start soon and which we expect to be robust, will be accompanied by the next corporate buyback blackout window. Buybacks have been a key driver of equity demand during the recent V-shaped equity rally. It's also worth pointing out that the replenishment of the Treasury General Account (TGA) – assuming the tax and spending bill is passed in the US – could produce temporary liquidity headwinds.

Still, we expect any resulting market pullbacks to be shallow. Investor positioning is light, with many still under-allocated to equities. This underexposure continues to create demand on dips, supporting the broader bullish trend.

Amid all the noise this year, there is one clear macro trend: a weaker US dollar. Foreign exchange markets are increasingly wary that the Fed will be pressured to ease funding conditions for the US government amid persistently high interest rates. Crucially, markets have not fully priced in the possibility that Powell could be replaced by a dovish loyalist. This would likely propel the Nasdaq 100, gold and crypto higher, while amplifying downward pressure on the dollar and front-end interest rates, even in a reflationary environment.

We maintain a preference for debasement trades, which to us means hard assets such as quality equities, precious metals, bitcoin and select commodities. Although the dollar appears tactically oversold and positioning is stretched, we may be at the beginning of a broader, structural bear market for the US dollar as history shows that currency trends tend to persist and overshoot.

Emerging markets stand to gain when three key conditions align: broad-based dollar weakness, a stable nominal growth environment and a dovish Fed. Over the next 6 to 12 months, we expect this trifecta to take shape. Accordingly, we are looking to increase our allocation to emerging markets.

As for strategic asset allocation, we would like to highlight the importance of diversifying portfolios with alternative investments. Long-duration bonds offer limited downside protection and could even be a major source of volatility over the next two years if fiscal excesses persist – a scenario that appears increasingly likely.

The broader US fiscal policy framework has clearly evolved from an agenda of “saving out of the debt” (recall DOGE) to “growing out of the debt” which aims to lift nominal GDP growth through tax cuts and deregulation above the fiscal deficit. The logical final stage of this progression would involve monetizing the debt through financial repression and quantitative easing-style interventions. In that context, we continue to believe that some form of yield curve control is the probable endgame for this phase of fiscal dominance. While not an immediate concern, this kind of policy framework could be increasingly likely by late 2027.

## Historical patterns indicate further gains in the coming months



A rare but historical bullish pattern has occurred: after a drawdown of -18%, the S&P 500 rallied to a new one-year high within just three months. This pattern has only developed a handful of times since 1927, and each instance has delivered strong forward returns.

Source: SubuTrade

Sources: Bloomberg, Morgan Stanley, Bank of America, Goldman Sachs, The Macro Compass, The Market Ear, Steno Research, 42Macro, JPM, Hightower Naples, Strategas, FT, LBBW, BCA Research, Finanz und Wirtschaft, Deutsche Bank



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