

Market Commentary

Summer Breeze

July 2025

Summary

- U.S. large-cap stocks, as measured by the S&P 500 Index, gained 2.2% in July while small-cap stocks rose 1.7%. U.S. intermediate-term bonds declined by 0.3%.
- The Fed's decision to hold interest rates steady led to two dissents—the most since 1993.
- Mega-cap tech stocks drove S&P 500 earnings growth expectations higher. Artificial intelligence continues to fuel record-high tech company capital expenditures while contributing to increased job cuts in the sector.
- A global minimum 10% tariff has been introduced by the U.S., and some countries will experience higher rates. With little retaliation, the effective U.S. tariff rate has risen to 8.85%, boosting tariff revenues and creating uncertainty around future inflation.
- July brought a summer breeze of calm to markets, but policy shifts, AI disruption, and changing consumer behavior signal a more complex rest of the year.

Overview

U.S. large-cap stocks, as measured by the S&P 500 Index, gained 2.2% in July, marking the third consecutive month of gains. The Russell 2000 Index of U.S. small-cap stocks ended the month up 1.7%. In contrast, U.S. intermediate-term bonds, represented by the Bloomberg U.S. Aggregate Bond Index, finished July roughly flat, down 0.3%.

Preliminary second-quarter GDP estimates showed that the U.S. economy grew at an annualized 3.0% quarter-over-quarter—a notable improvement from the 0.5% contraction reported in the first quarter. Consumer and government spending were the main drivers of this recovery.¹ Consumer spending rose 1.4%, compared to 0.5% in the first quarter, while government spending increased by 0.4%, reversing a 0.6% decline. However, not all signals were strong: the ISM Manufacturing PMI remained in contractionary territory in July, with a reading of 48. The employment component within manufacturing dropped to its lowest level since July 2020. According to the Institute for Supply Management, “for every comment on hiring, there were two on reducing headcounts.”² While the ISM Services PMI showed service sector activity continuing to expand, the prices paid component rose to 69.9% in July—the highest reading since October 2022.³ Tariffs and tariff-related costs were cited as the key reason for rising costs.³

The Federal Reserve held interest rates steady at 4.25% – 4.50% at the July 30 Federal Open Market Committee (FOMC) meeting. The decision generated two dissents, the most since 1993. Fed Governors Christopher Waller and Michelle Bowman favored a 0.25% rate cut; both cited labor market concerns as reasons for their dissent.⁴ In a statement on August 1, Waller noted:

“Data suggest that the downside risks to the labor market have increased. With underlying inflation near target and the upside risks to inflation limited, we should not wait until the labor market deteriorates before we cut the policy rate...I believe that the wait-and-see approach is overly cautious... and could lead to policy falling behind the curve.”⁵

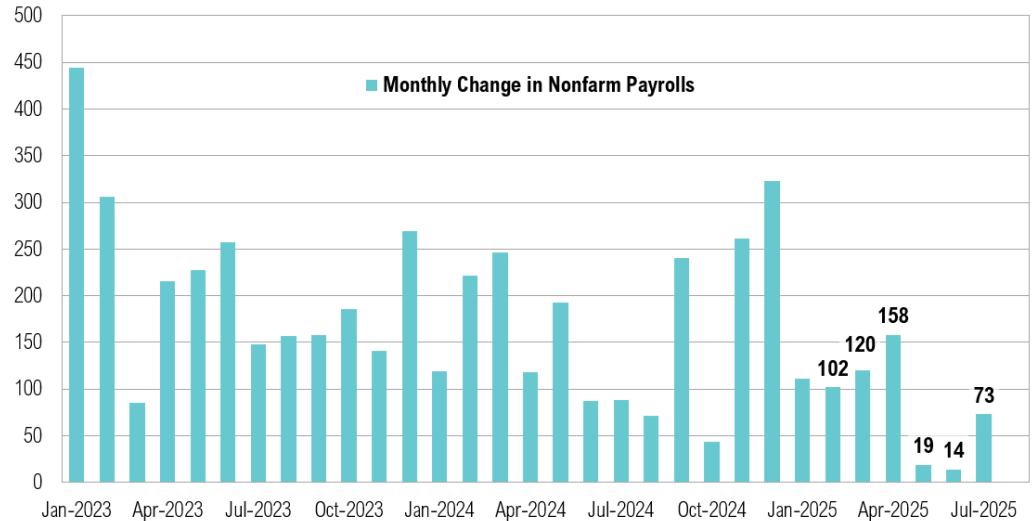
Consumer and government spending were the main drivers of second quarter growth

The FOMC decision to keep interest rates unchanged generated the most dissents since 1993

Both Waller and Bowman's concerns were validated by the July jobs report, released on August 1. The U.S. added 73,000 jobs in the month, missing expectations by 31,000.⁶ More significant, there were notable downward revisions to the prior two months: May and June payrolls were revised down by a combined 258,000 jobs—the largest two-month revisions ever outside of the 2020 pandemic.^{6,7}

Payroll Revisions to May and June Effectively Wipe Out Recent Job Gains

Monthly Change in Nonfarm Payrolls, Thousands



Source: Bloomberg, Bureau of Labor Statistics

May and June saw the largest two-month revisions ever outside of the 2020 pandemic

After easing to 2.3% year-over-year in May, headline inflation edged back up to 2.7% in June. Although the inflationary impact of new tariffs has so far been more muted than expected, price increases are becoming more visible in specific categories. The price for household furnishings rose 1% month-over-month in June, the highest since January 2023. Toy prices climbed 1.4% for the second consecutive month, and major appliance prices jumped 2.3%, the highest increase since January 2024. Despite inflation pressures on some goods, other areas appear to be experiencing easing pricing pressures. For example, housing inflation (which makes up over 30% of the inflation calculation) continues to ease. In June, shelter inflation increased by 0.2%, the lowest since February 2021.⁸ Despite remaining near all-time-highs, national average home prices in some major cities (Dallas, San Francisco, and Seattle) have started to decline.⁹ Further, the cost of renting continues to decline, dropping nearly 2% year-over-year in May across the 50 largest metro areas.¹⁰ Easing rent prices point to potentially slower shelter inflation and may help ease headline inflation in the coming months.

Easing rent prices point to potentially slower shelter inflation

The FOMC is now on a “summer break” and will reconvene on September 17. In the interim, policymakers will receive two more inflation and employment reports, which will further inform their rate decisions. For context, when the Fed cut interest rates by 0.5% in September 2024, headline inflation was at 2.6% year-over-year, and the most recent available jobs report at the time (August 2024) showed the U.S. economy adding a modest 71,000 new jobs. Arguably, current conditions are just as supportive of an interest rate cut as they were in September 2024. Market expectations for a 0.25% interest rate cut in September skyrocketed from 38% to 88% following the July jobs report.¹¹

Market expectations for a 0.25% interest rate cut in September skyrocketed from 38% to 88% following the July jobs report

Summer Breeze

From its April 8 low through July 31, the S&P 500 gained 27%

Markets spent most of July in a summery mood. On July 28, the S&P 500 set a record high, reaching 6,388 for the first time. From its April 8 low through July 31, the index gained 27%. U.S. small-cap stocks also rebounded strongly, rising 26% over the same period. Although it is still more than 6% below its all-time high, the small-cap index ended July just 0.1% in the red for the year.

This year's "summer slowdown" (a summertime phenomenon where the stock market exhibits lower trading volumes and price volatility) was reflected in the muted movement of the CBOE Volatility Index (or VIX), which measures market expectations for volatility. Despite ongoing tariff negotiations and a flurry of executive orders (15 in total), the VIX averaged just 16.4 in July, well below the five-year average of 20.1 and the year-to-date average of 20.4. It reached a low of 14.9 on July 25.¹² For context, the lowest-ever VIX reading was 9.5, recorded on September 29, 2017.¹²

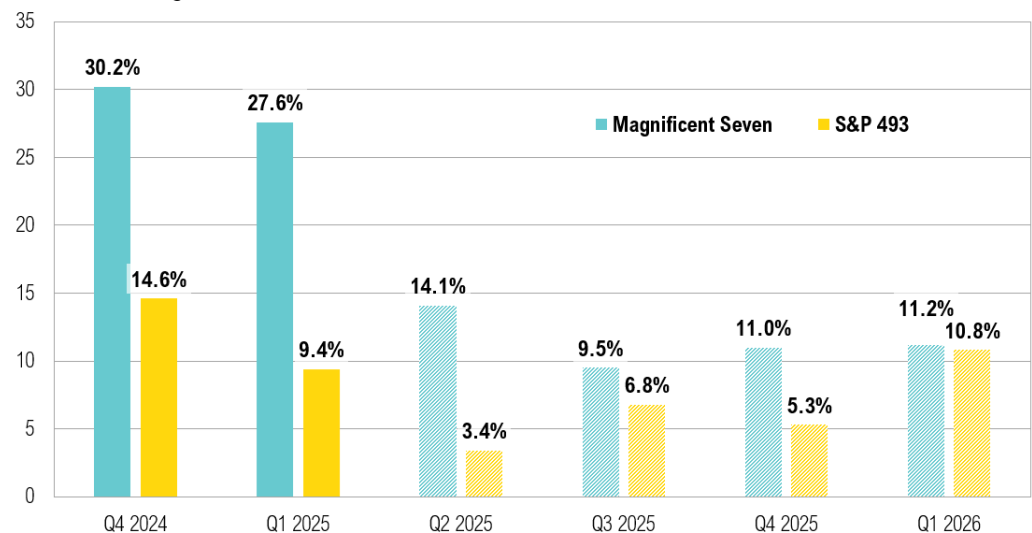
Strong earnings from mega-cap tech helped push S&P 500 earnings growth expectations higher

Corporate earnings helped underpin the market's strong performance. Through the end of July, year-over-year second-quarter earnings growth expectations for the Russell 2000 Index rose to 66.4%.¹³ Over 70% of small-cap companies beat second-quarter earnings expectations.¹³ Full-year S&P 500 earnings growth expectations steadily rose over the month, from 9.0% to 9.9%, buoyed by better-than-expected earnings results from U.S. large-cap companies.¹⁴ Perhaps unsurprisingly, the Magnificent Seven group of mega-cap technology companies (Alphabet, Amazon, Apple, Microsoft, Meta, Nvidia, and Tesla) continue to dominate the growth picture. For the second quarter, this group is expected to report earnings growth of 14%, compared to just 3.4% for the other 493 S&P 500 companies.¹⁵ This trend is expected to persist throughout the rest of the year, and the Magnificent Seven stocks are projected to deliver 9.5% and 11.0% year-over-year earnings growth in the third and fourth quarters of 2025 and 11.2% in the first quarter of 2026.¹⁵ The rest of the S&P 500 is also expected to see earnings growth improve. Forecasted year-over-year growth is expected to reach 6.8%, 5.3%, and 10.8% over the next three quarters.¹⁵

Mega-cap tech aside, earnings growth for the other 493 S&P 500 companies is expected to improve

The Magnificent Seven Continues to Dominate Earnings Growth

S&P 500 Earnings Growth Estimates, Y/Y %



Source: FactSet

AI-related capex is at a record high, with executives signaling more to come

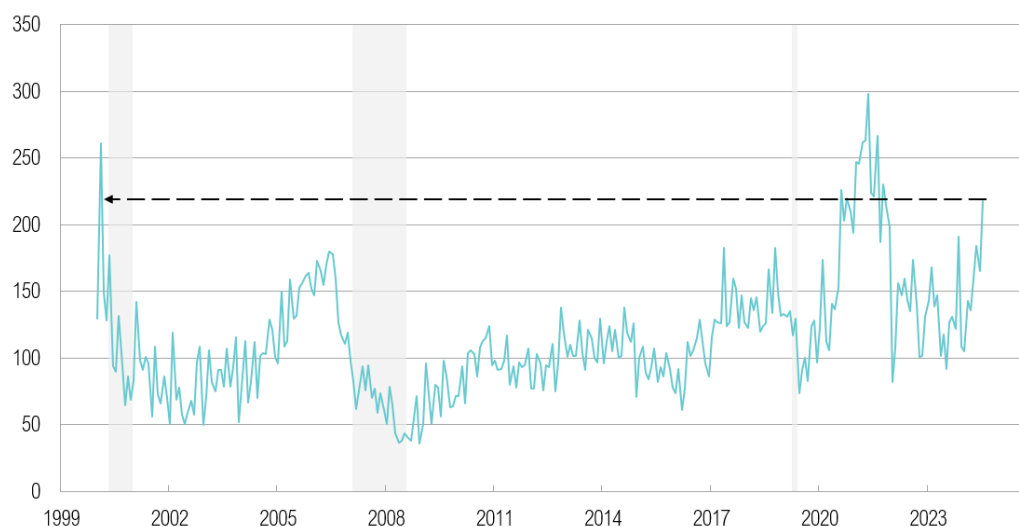
Capital expenditure trends reflect this tech-led momentum. Mega-cap firms are continuing to ramp up investment in artificial intelligence (AI) infrastructure. Spending in 2025 is already at record highs, and executives have signaled more to come. During its second-quarter earnings call on July 23, Alphabet said it expects to spend \$85 billion on capex in 2025—\$10 billion more than its earlier estimate of \$75 billion.¹⁶ In their second quarter earnings call, Meta's CFO noted:

*"We currently expect another year of similarly significant capex dollar growth in 2026 as we continue aggressively pursuing opportunities to bring additional capacity online to meet the needs of our AI efforts."*¹⁷

AI has started to drive shifts in the labor market. Job cuts in July rose to 62,075—the second-highest for a July in the past decade, behind only 2020. Technology firms led the way. According to Challenger, Gray & Christmas, AI and tariffs were the most commonly cited reasons for layoffs. Year-to-date, tech companies have announced 89,251 job cuts (up 36% year-over-year) with 10,375 of those directly attributed to artificial intelligence.¹⁸ At the same time, the JOLTS report showed job openings in the tech sector increasing by 4.1% in the first six months of 2025, the largest six-month jump in history—reflecting the shifting priorities for tech businesses.¹⁹

Apart from 2020, Tech Job Openings are at the Highest Since the Tech Bubble

Information Technology Sector Job Openings, Thousands



Source: Bloomberg. As of 6/30/2025.

Tech sector job cuts and job openings reflect shifting priorities for these businesses

Also in July, President Trump signed 15 executive orders, including the One Big Beautiful Bill Act (OBBBA) on July 4, and two orders related to furthering U.S. artificial intelligence and data center advancements.²⁰ Trade policy was another major focus. As of the August 1 deadline, only a minority of countries had finalized new trade agreements.²¹ The administration introduced a global minimum 10% tariff, along with targeted country-specific rates aimed at nations with large trade surpluses with the U.S.

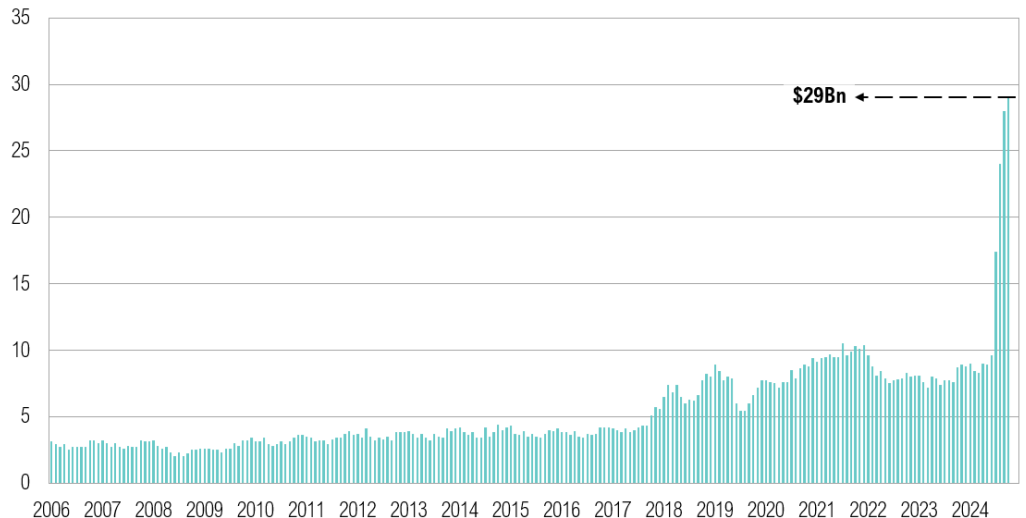
Trade agreements have been reached with, amongst others, Japan and the European Union

Trade agreements secured this far—with the European Union, Japan, South Korea, the United Kingdom, Vietnam, Indonesia, and the Philippines—are notably U.S.-friendly. For example, the EU has committed to investing \$600 billion in the U.S. and purchasing \$750 billion in U.S. energy products.²² South Korea has said that it will invest \$200 billion in semiconductors and buy \$100 billion in U.S. energy.²³ Japan pledged \$550 billion in investment and agreed to open its markets to American cars, rice, and agricultural goods, although these pledges are non-binding and rice commitments remain within existing

quotes.^{24,25} The effective U.S. tariff rate has climbed to 8.85%, and tariff revenues are growing.²⁶ A record \$29 billion was collected in July, bringing the fiscal year-to-date total to \$151 billion.²⁷ The additional revenue could help partially offset the \$1.34 trillion federal deficit, which is expected to widen further due to the OBBBA.²⁸

July 2025 Saw a Record \$29Bn in Customs and Excise Taxes Collected

U.S. Treasury Deposits: Customs & Certain Excise Taxes, \$Bn



Source: Bloomberg. As of 7/31/2025.

Tariff revenue could help partially offset the fiscal deficit

Retail investors have been unusually active in 2025, and inflows picked up sharply after President Trump announced new tariffs in early April. Over the past three months, their share of total individual stock trading has reached the highest levels since the meme-stock peaks of 2020 and 2021.^{29,30} Retail traders tend to chase high-performing, high-value names with a short-term mindset.

National average gas prices are at the lowest level since the summer of 2021

Outside of markets, it appears that (so far) summer vacations in 2025 have been a little cooler than in recent years. According to the Bureau of Economic Analysis, the number of people who took time off work in July dropped to its lowest level since the pandemic.³¹ Bank of America reported a sharp drop in big-ticket airline spending, to its lowest since June 2021, as many consumers opted for more affordable travel.³² Still, over 70% of survey respondents said they planned to travel over the summer, with domestic road trips topping the list.³³ That trend aligns with falling gas prices and the recent jump in auto purchases, driven by consumers seeking to front-run impending tariffs. At \$3.15 for a gallon of regular gas, national average gas prices are at the lowest level since the summer of 2021.³⁴ And yet, air travel hasn't vanished. As Delta Air President Glen Hauenstein noted in the company's recent earnings call:

*"We had our highest cash sales day for the month of July in a 100-year history yesterday [July 9]. So advanced bookings are doing well. I think at the beginning, when people were fearful, we saw the further out bookings going away. We see those starting to return again and hopefully, those trends continue."*³⁵

July brought a summer breeze of calm to markets

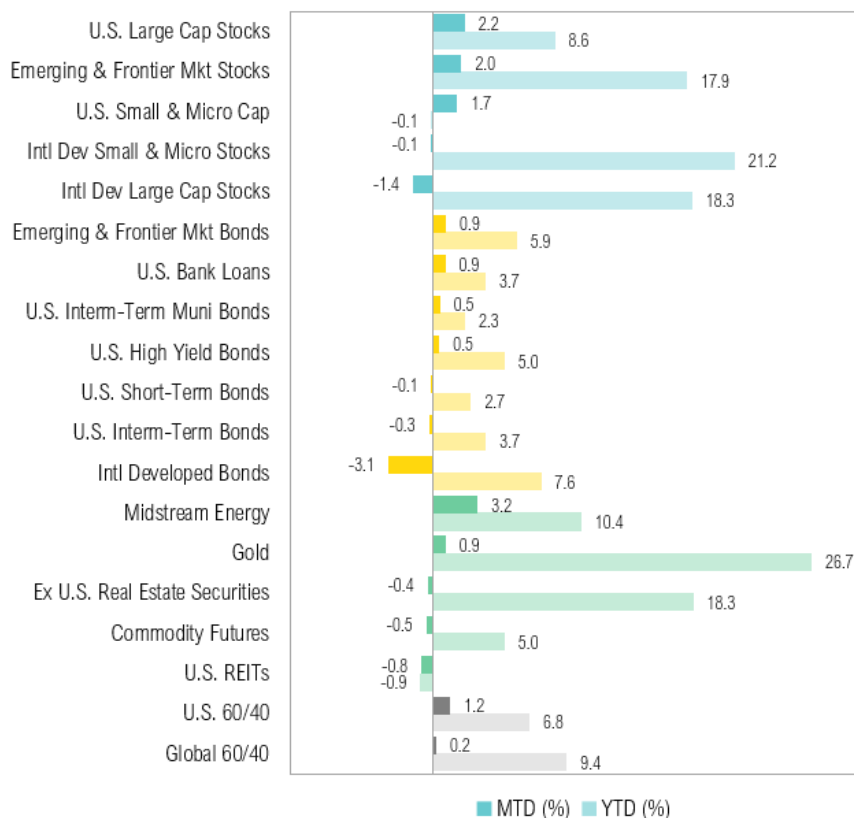


Source: SpringTide, Noah Kroese

Markets

U.S. large-cap stocks ended July up 2.2%, outperforming their foreign peers by 3.6%, as international developed market stocks ended the month down 1.4%. U.S. small-cap stocks ended the month up 1.7% while international developed market small cap stocks ended the month flat.

July 2025 Key Market Total Returns



Source: Bloomberg

U.S. large-cap stocks outperformed foreign peers by 3.6%

Gold remains a top performer year-to-date, gaining 27% since January

Policy shifts, AI disruption, and changing consumer behavior signal a more complex rest of the year

Investors should maintain a healthy level of risk, tilted to areas with fundamental and policy tailwinds

Gold, which remains a top performer year-to-date (gaining 27% since January), ended the month up 0.9%, at \$3,289 per ounce. Copper prices plummeted by 18% on July 30 as the U.S. implemented 50% tariffs on imports of semi-finished copper products, but not the raw material itself.³⁶ West Texas Intermediate (WTI) crude oil prices traded between \$65 per barrel and \$70 per barrel throughout the month, while national average gas prices remained at a three-year low for this time of year. U.S. crude inventories sit at 426.7 million barrels—around 6% below the five-year seasonal average.³⁴

Looking Forward

July brought a summer breeze of calm to markets, even as deeper undercurrents—policy shifts, AI disruption, and evolving spending patterns—remain key forces shaping markets into year end. Fiscal support for the economy remains strong, and markets now expect rate cuts at the next FOMC meeting. But any growth will not necessarily be evenly distributed. Certain areas, like healthcare, remain under political and regulatory scrutiny—evidenced by declining earnings expectations and most recently by the most-favored nation (MFN) letters sent out by the Trump administration in late July. Still others, such as infrastructure and utilities, are direct beneficiaries of secular trends.

Bond yields, which we have long viewed as the potential constraint on fiscal excesses, have remained contained, partially due to softening in the labor market. But the signal may be muddled. AI is reshaping the labor market, but it also may deliver productivity enhancements that could support corporate margins in some areas. As Microsoft CFO Amy Hood noted in their second-quarter earnings call, “We expect Q1 capital expenditures to be over \$30 billion...driven by the continued strong demand signals we see.”³⁷ Inflation, meanwhile, continues to flow through via tariffs and targeted goods, but there are offsets, including low energy prices and a cooling in housing inflation. Although most risky assets are substantially higher than their April lows and their valuations are more elevated, we still believe investors should maintain a healthy level of risk—balanced, not excessive, and tilted to areas with fundamental and policy tailwinds.

Disclosures

The material shown is for informational purposes only. Any opinions expressed are current only as of the time made and are subject to change without notice. This report may include estimates, projections or other forward-looking statements; however, forward-looking statements are subject to numerous assumptions, risks, and uncertainties, and actual results may differ materially from those anticipated in forward-looking statements. As a practical matter, no entity is able to accurately and consistently predict future market activities.

Additionally, please be aware that past performance is not a guide to the future performance of any investment, and that the performance results and historical information provided displayed herein may have been adversely or favorably impacted by events and economic conditions that will not prevail in the future. Therefore, it should not be inferred that these results are indicative of the future performance of any strategy, index, fund, manager or group of managers.

The graphs and tables making up this report have been based on unaudited, third-party data and performance information provided to us by one or more commercial databases. While we believe this information to be reliable, Blue Line Capital bears no responsibility whatsoever for any errors or omissions. Index benchmarks contained in this report are provided so that performance can be compared with the performance of well-known and widely recognized indices. Index results assume the re-investment of all dividends and interest. Moreover, the information provided is not intended to be, and should not be construed as, investment, legal or tax advice. Nothing contained herein should be construed as a recommendation or advice to purchase or sell any security, investment, or portfolio allocation. This presentation is not meant as a general guide to investing, or as a source of any specific investment recommendations, and makes no implied or express recommendations concerning the manner in which any client's accounts should or would be handled, as appropriate investment decisions depend upon the client's specific investment objectives.

Terms of Use

This report is intended solely for the use of its recipient. There is a fee associated with the access to this report and the information and materials presented herein. Re-distribution or republication of this report and its contents are prohibited. Blue Line Capital, LLC is a registered investment adviser with the Securities and Exchange Commission; registration does not imply a certain level of skill or training. For more detail, including information about Blue Line Capital's business practices and conflicts identified, please refer to Blue Line Capital's Form ADV Part 2a and Form CRS at: <https://bluelinecapitalwealth.com>

Performance Disclosures

All market pricing and performance data from Bloomberg, unless otherwise cited. Asset class and sector performance are gross of fees unless otherwise indicated.

Asset Class Definitions

Asset class performance was measured using the following benchmarks: U.S. Large Cap Stocks: S&P 500 TR Index; U.S. Small & Micro Cap: Russell 2000 TR Index; Intl Dev Large Cap Stocks: MSCI EAFE GR Index; Emerging & Frontier Market Stocks: MSCI Emerging Markets GR Index; U.S. Interm-Term Muni Bonds: Bloomberg 1-10 (1-12 Yr) Muni Bond TR Index; U.S. Interm-Term Bonds: Bloomberg U.S. Aggregate Bond TR Index; U.S. High Yield Bonds: Bloomberg U.S. Corporate High Yield TR Index; U.S. Bank Loans: S&P/LSTA U.S. Leveraged Loan Index; Intl Developed Bonds: Bloomberg Global Aggregate ex-U.S. Index; Emerging & Frontier Market Bonds: JPMorgan EMBI Global Diversified TR Index; U.S. REITs: MSCI U.S. REIT GR Index, Ex U.S. Real Estate Securities: S&P Global Ex-U.S. Property TR Index; Commodity Futures: Bloomberg Commodity TR Index; Midstream Energy: Alerian MLP TR Index; Gold: LBMA Gold Price, U.S. 60/40: 60% S&P 500 TR Index; 40% Bloomberg U.S. Aggregate Bond TR Index; Global 60/40: 60% MSCI ACWI GR Index; 40% Bloomberg Global Aggregate Bond TR Index.

Citations

1. Bureau of Economic Analysis: <https://www.bea.gov/sites/default/files/2025-07/gdp2q25-adv.pdf>
2. ISM: <https://www.ismworld.org/supply-management-news-and-reports/reports/ism-report-on-business/pmi/july/>
3. ISM: <https://www.ismworld.org/supply-management-news-and-reports/reports/ism-report-on-business/services/july/>
4. CNBC: <https://www.cnbc.com/2025/08/01/fed-governors-bowman-waller-explain-their-dissents-say-waiting-to-cut-rates-threatens-economy.html>
5. Federal Reserve: <https://www.federalreserve.gov/newsevents/speech/waller20250801a.htm>
6. Bureau of Labor Statistics: <https://www.bls.gov/news.release/empstat.nr0.htm>
7. MacroMicro: <https://en.macromicro.me/charts/99068/nonfarm-payrolls-monthlychange-2months-revisions>
8. FRED: <https://fred.stlouisfed.org/series/CUSR0000SAH1>
9. FRED: <https://fred.stlouisfed.org/series/CSUSHPINSA#>
10. Realtor.com: <https://www.realtor.com/research/may-2025-rent/>
11. CME: <https://www.cmegroup.com/markets/interest-rates/cme-fedwatch-tool.html>
12. FRED: <https://fred.stlouisfed.org/series/VIXCLS>
13. Lipper Alpha: <https://lipperalpha.refinitiv.com/2025/07/russell-2000-earnings-dashboard-25q2-jul-31-2025/>
14. FactSet: https://advantage.factset.com/hubfs/Website/Resources%20Section/Research%20Desk/Earnings%20Insight/EarningsInsight_080125.pdf
15. FactSet: <https://insight.factset.com/are-magnificent-7-companies-still-top-contributors-to-earnings-growth-for-the-sp-500-for-q2>
16. Alphabet: <https://abc.xyz/assets/bc/0f/01ca2b344c3b8a4efaa3783f9fdf/2025-q2-earnings-transcript.pdf>
17. Meta: https://s21.q4cdn.com/399680738/files/doc_financials/2025/q2/META-Q2-2025-Earnings-Call-Transcript.pdf
18. Challenger: <https://www.challengergray.com/blog/summer-lull-ends-july-job-cuts-spike-tech-ai-tariffs-blamed/>
19. FRED: <https://fred.stlouisfed.org/series/JTU5100JOL>
20. White House: <https://www.whitehouse.gov/presidential-actions/executive-orders/>
21. CNBC: <https://www.cnbc.com/2025/07/31/trumps-aug-1-tariff-deadline-those-who-have-and-havent-signed-deal.html>
22. Reuters: <https://www.reuters.com/business/autos-transportation/whats-trumps-trade-deal-with-europe-2025-07-27/>
23. CNN: <https://edition.cnn.com/2025/07/30/business/us-south-korea-trade-deal>
24. Bloomberg: <https://www.bloomberg.com/news/articles/2025-07-23/japan-s-trade-deal-a-positive-surprise-for-markets-analysts-say>
25. CNN: <https://edition.cnn.com/2025/07/22/business/japan-trade-agreement-us>
26. Bloomberg data series
27. Bloomberg data series
28. Penn Wharton Budget Model: <https://budgetmodel.wharton.upenn.edu/issues/2025/2/26/tariff-revenue-simulator>
29. Citadel Securities: <https://www.citadelsecurities.com/news-and-insights/global-market-intelligence-gmi-august-views/>
30. Reuters: <https://www.reuters.com/markets/us/retail-replaces-smart-money-wall-street-rocket-fuel-2025-07-29/>
31. Washington Post: <https://www.washingtonpost.com/business/2025/08/02/trump-policies-impact-summer-travel/>
32. Bank of America: <https://institute.bankofamerica.com/content/dam/economic-insights/consumer-checkpoint-july-2025.pdf>
33. Bank of America: <https://institute.bankofamerica.com/content/dam/economic-insights/vacation-nation.pdf>
34. AAA: <https://gasprices.aaa.com/pump-prices-stay-in-their-lane-as-august-begins/>
35. Delta Air: https://s2.q4cdn.com/181345880/files/doc_earnings/2025/q2/transcript/CORRECTED-TRANSCRIPT_-_Delta-Air-Lines-Inc-DAL-US-Q2-2025-Earnings-Call.pdf
36. Bloomberg: <https://www.bloomberg.com/news/articles/2025-08-05/trump-s-copper-tariffs-apply-to-15-billion-of-products-so-far>
37. Microsoft: <https://view.officeapps.live.com/op/view.aspx?src=https://cdn-dynmedia-1.microsoft.com/is/content/microsoftcorp/TranscriptFY25q4>