

KKR

# Insights

15.3

Global  
Macro Trends  
July 2025



# Make Your Own Luck

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Mid-Year Outlook for 2025

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# Make Your Own Luck

## Mid-Year Outlook for 2025

Without question, the first half of 2025 has been an eventful one. The introduction of DeepSeek in January, to tense trade negotiations in the spring, to stickier inflation, to a U.S. sovereign downgrade, to a U.S. airstrike in Iran in June, have all served as stark reminders that a new world order, including a notable transition from benign globalization to one of great power competition, continues to unfold. For some time, we have been calling this shift in the investment landscape a *Regime Change*, one in which an investor needs to think differently about where, when, and how to allocate assets, including the changing role of both Alternatives and government bonds in a portfolio. Importantly, though, despite all this perceived turbulence, financial risk assets, especially outside the U.S., have kept climbing, as the overall macro landscape has rewarded those who stuck to our ‘Glass Half Full’ thesis for the past few years. As we look ahead at KKR, we remain positive. To be sure, we expect more market drawdowns than in the past, but our ‘Glass Still Half Full’ thinking is that attractive financial conditions, a global easing cycle, ongoing productivity gains, and lack of net issuance—coupled with some incredibly powerful investment themes—will continue to drive this cycle both further and longer than many think. That said, we do start to want to build in some additional cushion in our approach in 2H25, and as such, we are advocating more allocations that allow investors to ‘Make Their Own Luck’ through, for example, control positions with operational upside in Private Equity, senior slices of Credit amidst wide dispersions, and/or Real Assets with long-dated, inflation-linked contracts that can reprice alongside rising nominal GDP. We also want to harness volatility and uncertainty to our advantage by using any periodic dislocations to lean heavily into our major macro investment themes, including the Security of Everything, Productivity and Worker Retraining, the shift from Capital Heavy to Capital Light, and Collateral-Based Cash Flows. Our bottom line: against a still favorable backdrop for financial markets, we want to tilt our portfolios to gain more exposure to operational leverage stories and macro tailwinds that help us to better control investment outcomes than in the past.

You never know how things are going to change.  
You’ve got to be ready when they change.  
And you have to be prepared to get lucky.

— **Scott Bessent**, 79th Secretary of the Treasury of the United States

From almost any vantage point, the first half of 2025 has been a wild ride, with a plethora of unexpected twists and turns. Consider the following events that all happened in just the past few months. DeepSeek-R1 was officially rolled out on January 20th, setting the stage for a potential market shock to the dominance of the Mag7. Soon after, President Trump announced 25% tariffs on Mexico and Canada as well as 10% on China. This was quickly followed by broad-based tariffs across 60 countries on 'Liberation Day', April 2nd, though ongoing negotiations continue. Then, on May 16th, Moody's downgraded U.S. government debt, marking only the second time since 1917 that the U.S. no longer holds a top-tier rating from at least one of the three major credit rating agencies. Most recently, Israel and the United States joined forces in a bid to deter Iran's nuclear program, while Europe agreed to raise defense spending to 5% of GDP after years of missing the two-percentage point target, and the U.S. Congress and President Trump signed into law the One Big Beautiful Bill Act which makes permanent the 2017 lower corporate tax rates, as well as adding other provisions aimed to enhance economic growth.

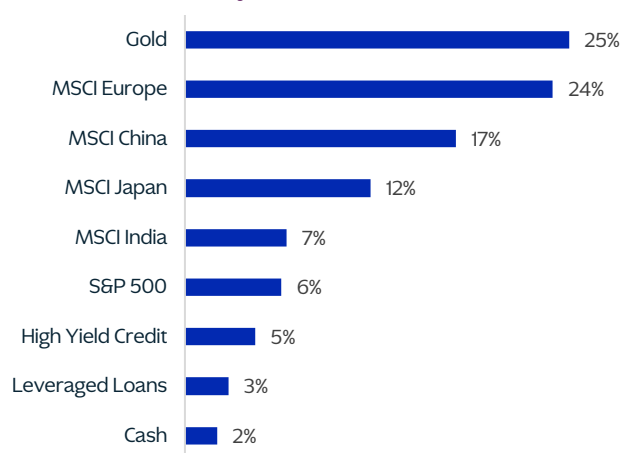
However, despite all these potentially consequential events, the global capital markets—especially outside of the United States—have actually delivered solid results year-to-date. One can see this in *Exhibit 1*. Simply stated, it has paid to maintain a 'Glass Still Half Full' approach, even amidst all the volatility. For our nickel, we see it as a continuation of our view that an incredibly positive technical backdrop, including a weaker dollar, lower global rates, and the lack of supply, would help to support what at best could be described as mediocre fundamentals.

Where do we go from here? Our message remains to stay invested as well as to stay the course by leveraging our top-down *Regime Change* framework and investing behind our priority macro trends. Against the current backdrop, we think that many investors may still be underestimating that financial conditions remain quite easy. One can see this in *Exhibit 2*, which shows that valuations should remain firm in the environment we continue to envision. Another input where we are more constructive than the consensus is the reality that overall net debt levels actually remain constant (*Exhibit 69*). This insight is likely underappreciated by the market, we believe. To be sure, sovereign balance sheets have

expanded meaningfully, but corporate and consumer leverage remains well-behaved. This unusual reality has provided a supportive backdrop for credit issuance, even in the face of elevated risk-free rates amidst the threat of higher fiscal deficits. As such, what we're seeing is that tighter spreads are doing real work to cushion the rise in yields, particularly in an economy that is still growing above trend in nominal terms.

**Exhibit 1:** Despite a Slew of Unexpected Headlines, the Glass Has Been More Half Full Than Many Were Expecting

#### YTD Total Return by Asset Class, %



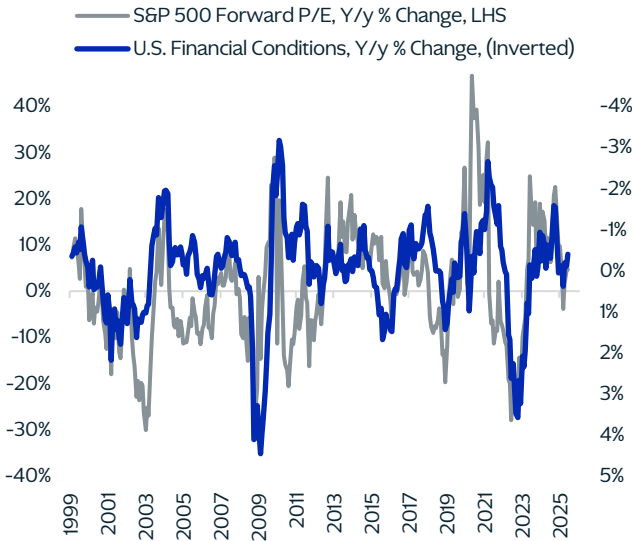
Equity indices refer to MSCI Total Return (USD) unless otherwise specified, HY refers to the BofA U.S. High Yield Index, Leveraged Loans refers to Morningstar U.S. Leveraged Loan Index, cash refers to 3m T-bills. Data as at June 30, 2025. Source: Bloomberg, KKR Global Macro & Asset Allocation analysis.

Where do we go from here?  
Our message remains to stay invested as well as to stay the course by leveraging our top-down *Regime Change* framework and investing behind our priority macro trends.



**Exhibit 2: Despite Negative Sentiment, the Current Environment Is Actually One of Easier Financial Conditions and Better Price to Earnings Ratios**

**S&P 500 NTM P/E vs. U.S. Financial Conditions, %**



Data as at June 30, 2025. Source: S&P, GS Financial Conditions Index.

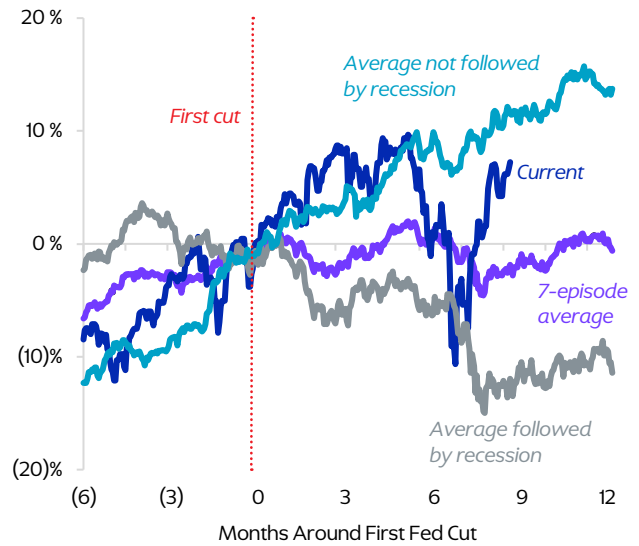
Looking at the bigger picture, on many of the days where we are feeling more optimistic about market conditions, we remind ourselves that there are several parts of today’s investment landscape that ‘rhyme’ a lot with the 1990s. In particular, just as the Internet revolution drove massive capital inflows and inspired enthusiasm, today’s wave of innovation—centered around artificial intelligence, automation, and advanced semiconductors—is fueling a similar tech-driven boom. In addition, market gains once again are disproportionately driven by a select group of dominant technology firms, echoing the rise of firms like Microsoft, Cisco, and Intel during the dot-com era. Finally, investor optimism is once again grounded in expectations of a long-term productivity surge, with equity valuations expanding in anticipation of future growth rather than current earnings.

However, there are plenty of concerns on which to focus, including significant structural shifts in trading relationships and the flow of funds that could challenge the traditional, synchronized nature of the global economy. Meanwhile, inflation in the United States isn’t slowing as quickly as many would like, a backdrop that is shaping consumer sentiment and influencing voter behavior in profound

ways. Geopolitics too, are increasingly impacting sentiment and introducing risks that are far more difficult to quantify than in the past. As General (Retired) David Petraeus, head of our KKR Global Institute (KGI), often reminds us, we have clearly transitioned from an era of benign globalization to one defined by great power competition. Not surprisingly, against this backdrop, we continue to argue that we should all expect an asynchronous global recovery, one that is characterized by both rolling recessions and rolling recoveries across different sectors throughout the cycle.

**Exhibit 3: Unless We Have a Recession (Not Our Base View), Fed Easing Cycles Usually Lead to Solid Market Returns**

**S&P 500 Returns Around the Start of Fed Cutting Cycles**

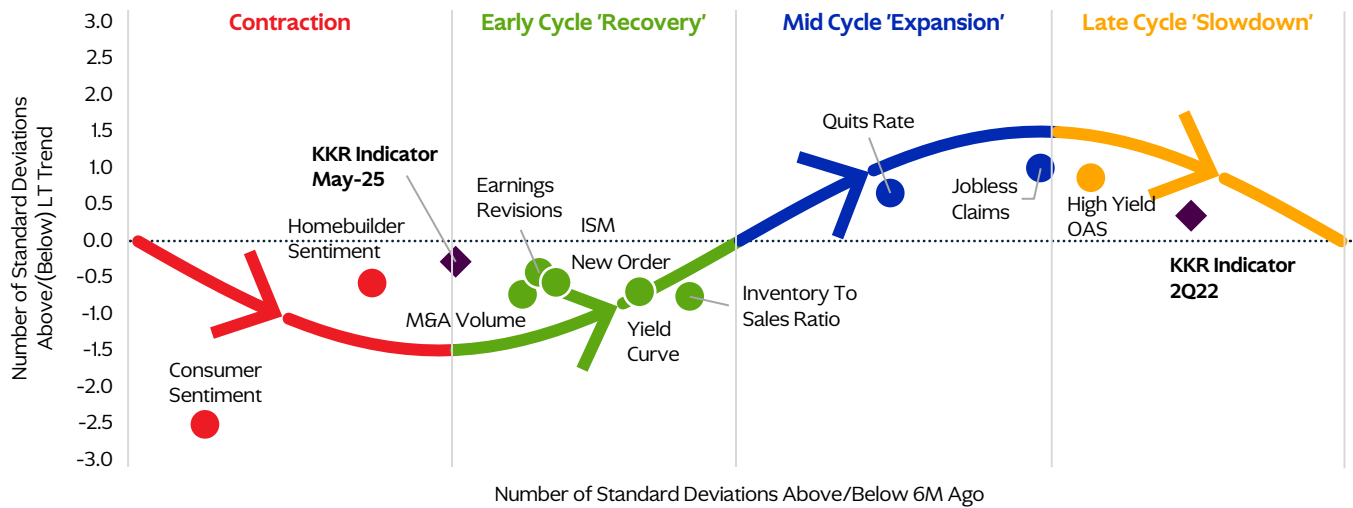


Data as at June 3, 2025. Source: Goldman Sachs Research, KKR Global Macro & Asset Allocation analysis.

Specifically, what were once seen as temporary negotiating tactics are now becoming embedded features of industrial and geopolitical strategy.

**Exhibit 4:** We Continue to See an Asynchronous Recovery Defined by Rolling Recoveries and Rolling Recessions

**KKR GMAA Cycle Indicator**

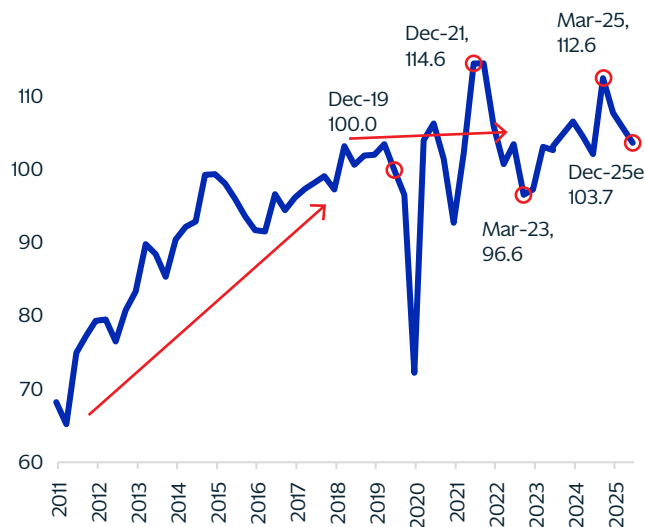


Data as at June 26, 2025. Source: U.S. Bureau of Economic Analysis, Haver Analytics, KKR Global Macro & Asset Allocation analysis.

**Exhibit 5:** True Economic Hard Landings Are Usually Caused by Housing and Inventory Issues. This Cycle Has Not Yet Been Marked by Excesses in Those Areas

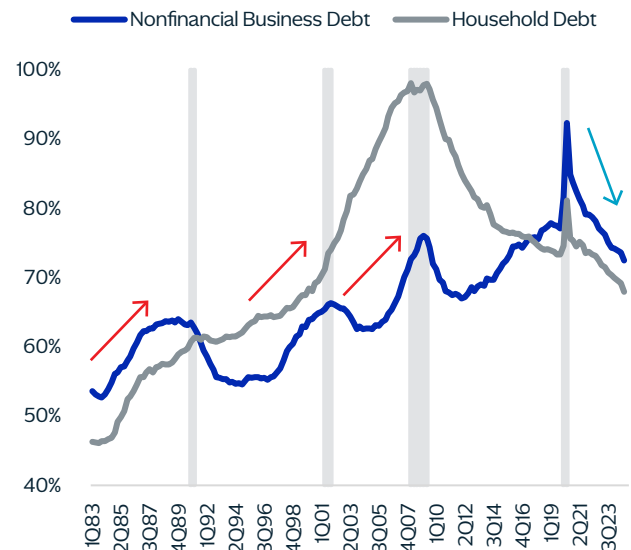
**Exhibit 6:** Business and Consumer Leverage Levels Have Not Increased This Cycle, Which Has So Far Helped to Offset the Excess Debt Issuance in the Government Sector

**Real Construction + Inventory Investment (4Q19=100)**



e = KKR GMAA estimates. Data as at June 10, 2025. Source: U.S. Bureau of Economic Analysis, Haver Analytics, KKR Global Macro & Asset Allocation analysis.

**U.S. Private Sector Leverage as a % of GDP**



Gray shading denotes recessionary quarters. Data as at June 10, 2025. Source: U.S. Bureau of Economic Analysis, Haver Analytics, KKR Global Macro & Asset Allocation analysis.

Finally, we expect to soon see the lagged effects of a higher resting rate for interest rates this cycle. For now, many floating-rate borrowers remain insulated, benefitting from pandemic-era rate hedges that are still rolling off. However, as those protections fade, interest burdens will begin to rise more materially. With the high yield index already trading in the mid-90s, and financial conditions tightening in the background, we think the pressure on the Fed to ease will build—not because the economy has cracked, but because the delayed impact of cumulative tightening starts to bind more visibly across credit markets.

Given all these cross currents as we approach the back half of the year and beyond, we have spent time as a team reflecting on the most important things to know about what has remained constant and what has changed in our thinking since last December.

The *net* issuance of IPOs, Leveraged Loans, and High-Yield bonds is currently at levels not seen since the recovery from the Global Financial Crisis. Importantly, this backdrop is unfolding at a time when many CIOs—particularly within insurance companies—are starved for fixed income products.

**What remains the same in our thinking since the end of last year, when we published *Glass Still Half Full*, is the following:**

1

**Capital markets are responding favorably to a global easing cycle.**

Though the Fed is still missing its inflation mandate more than its employment mandate, we think softer growth and incremental improvements in inflation will lead to gradual cuts later in 2025. We see this as a favorable shift, especially given the resilience we are seeing in labor markets, improving productivity, and a softening in price pressures. While the easing is unfolding asynchronously across other regions, we believe it is helping to reset risk premiums in a way that supports Equities and Credit, particularly in capital-intensive sectors and more idiosyncratic opportunities.

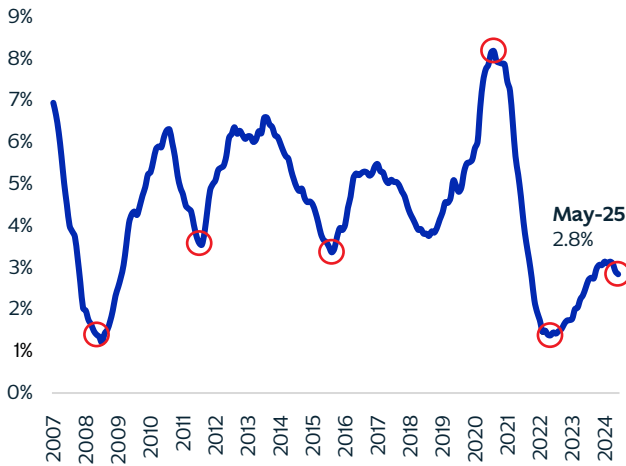
2

**A stellar technical backdrop has supported/bolstered markets nicely.**

The *net* issuance of IPOs, Leveraged Loans, and High-Yield bonds is currently at levels not seen since the recovery from the Global Financial Crisis (GFC). Importantly, this backdrop is unfolding at a time when many CIOs—particularly within insurance companies—are starved for fixed income products. Even as issuance remains subdued, U.S. companies are projected by Goldman Sachs to repurchase another trillion dollars or more of their own stock in 2025.

**Exhibit 7:** Our Liquidity Indicator Suggests We Are Still Recovering From Near-Trough Levels

**Capital Markets Liquidity (TTM) as a % of GDP (IPO, HY Bond, Leveraged Loan Issuance)**



Data as at May 31, 2025. Source: Preqin, Bank of America, Bloomberg, KKR Global Macro & Asset Allocation analysis.

**Exhibit 8:** Risk Assets Are Responding Favorably to the Idea of Fewer Tightenings and More Easings

**Percentage of Top 25 Central Banks Hiking**



Hiking/cutting rates defined as an increase in rates over the past three months. Data for U.S., JP, CN, AU, CA, E2, NZ, NO, SE, GB, JP, CH, IN, ID, KR, PH, TW, TH, VN, BR, CL, ZA, TR, IL, CZ, HU, PL. Data as at June 15, 2025. Source: Bloomberg, KKR Global Macro & Asset Allocation analysis.

# 3

Despite tariff-induced uncertainty, positive earnings momentum has continued.

Unlike the downturn in 2007, which was driven by both bank and consumer deleveraging, surging oil prices, and sharply wider credit spreads, much of the recent market volatility has been policy-related, which does not share those same attributes. In fact, despite recent policy and Middle East-related uncertainty, oil prices remain near the low end of their range for this cycle, and credit spreads have been the most coincident indicator in our long-standing Earnings Growth Leading Indicator (or EGLI model). Further, banks are flush with cash, and global policy rates are heading lower. **Importantly, the year-ahead growth signals we are getting from our EGLI model today have actually improved to +8% recently from +4% in the weeks immediately following ‘Liberation Day’.** More settled credit spreads and low energy prices have driven most of the recent improvements (See Exhibits 9 and 14, respectively, for more details). That said, we are watching oil prices closely (we are currently estimating \$65 per barrel in the model), as every \$10 increase in oil dents our EPS model at around 3-4%.

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# 4

## Our Regime Change thesis for asset allocation remains a high-conviction framework at KKR.

A new and important variable has emerged within our thesis: the prospect of a structurally weaker U.S. dollar. Coupled with our long-held view that the stock-bond correlation is shifting from negative to positive in this cycle, we think this development warrants investor attention.

# 5

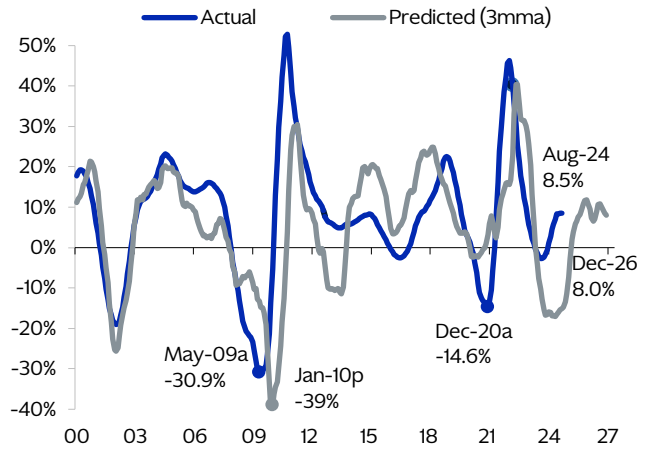
## We think that the KKR Global Institute’s long-held belief that the lines between geopolitics, politics, and economics are blurring, is only gaining momentum.

Increasingly in this world, geopolitics and politics are driving economics, and there is a merging of capital markets policy and national security policy as cross-border barriers to the flow of capital, data, technology, and people rise. Seen through this lens, key milestones such as Brexit and now ‘Liberation Day’ represent just the latest ‘textbook’ examples of the convergence that KGI has been suggesting.

Geopolitics and politics are driving economics, and there is a merging of capital markets policy and national security policy as cross-border barriers to the flow of capital, data, technology, and people rise.

**Exhibit 9:** Year-Ahead Growth Signals From Our EGLI Have Actually Improved to +8% Recently From +4% in the Weeks Immediately Following ‘Liberation Day’

### S&P 500 EPS Growth: 12-Month Leading Indicator



Our S&P 500 Earnings Growth Leading Indicator (‘EGLI’) is a combination of seven macro inputs that together, we think have significant explanatory power regarding the S&P 500 EPS growth outlook. Data as at July 2, 2025. Source: National Association of Realtors, ISM, Conference Board, Bloomberg, KKR Global Macro & Asset Allocation analysis.

**Exhibit 10:** The Forward-Looking Expected Range of Outcomes Will Likely Be Narrower. Therein Lies the Opportunity, We Believe, for Active Management

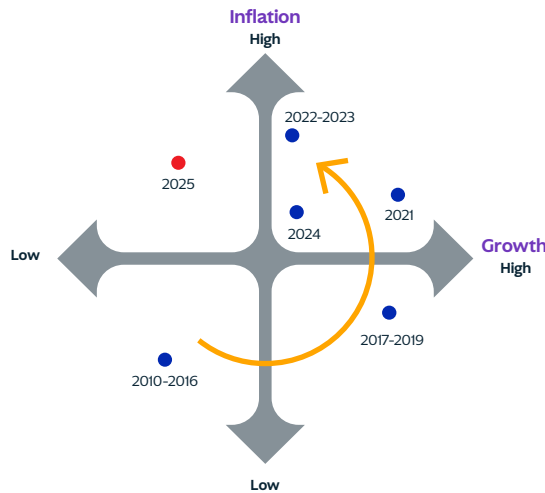
### Expected Return Range of Outcomes, %



Data as at May 31, 2025. Source: KKR Global Macro & Asset Allocation analysis.

**Exhibit 11:** We Have Moved From a Low Growth, Low Inflation Environment to One of a Higher Resting Heart Rate for Inflation This Cycle

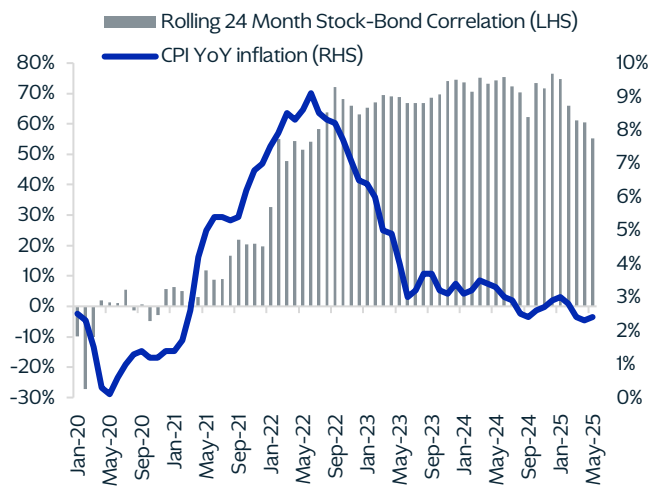
**Low and High Growth and Inflation Regimes**



Data as at April 5, 2025. Source: KKR Global Macro & Asset Allocation analysis.

**Exhibit 12:** This Time is Different, as We No Longer See the Stock/Bond Correlation as Negative. This Viewpoint Has Major Implications for Asset Allocation

**U.S. Stock-Bond Correlation and U.S. CPI, %**



Data as at May 31, 2025. Source: Bloomberg, KKR Global Macro & Asset Allocation analysis.

The following considerations have resulted in changes to our thinking:

1

Sustained bigger U.S. deficits may now require a greater ‘term’ premium by investors for owning American assets than we imagined at the start of the year.

Traditional factors influencing the term premium, including inflation expectations and monetary policy, are now being compounded by structural fiscal imbalances. This shift suggests that the term premium may remain elevated (*Exhibits 63 and 74*), reflecting the increased risks associated with long-term U.S. debt. In this context, our investment strategy emphasizes assets that offer protection against inflation and are linked to nominal GDP growth such as Infrastructure, Real Estate, and Asset-Based Finance, providing collateral-backed cash flows that are less sensitive to interest rate fluctuations. See Section IV, Frequently Asked Questions, for details.

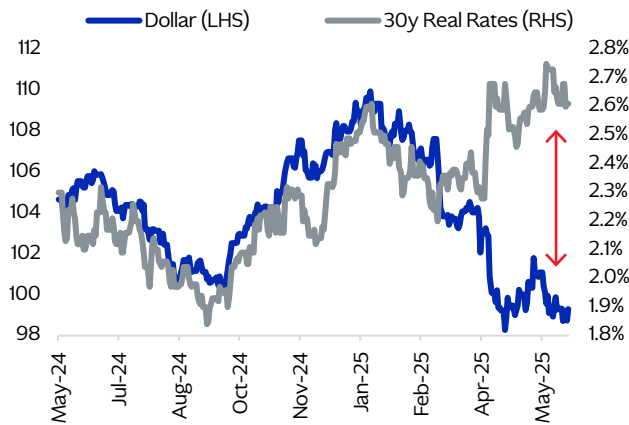
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In addition to growing deficits, the arrival of ‘Liberation Day’ also created a potentially more serious backdrop for U.S. dollar weakness.

Recent events—including oscillating tariff rates and political tensions between President Trump and Fed Chair Powell—underscore how a depreciating dollar in tandem with Equities selling off and bond prices declining can act as a destabilizing force within this evolving macro environment. See Section III, Capital Markets, for details.

**Exhibit 13: A Weaker Dollar and Higher Long-Term Bond Yields Are Signaling a New Regime**

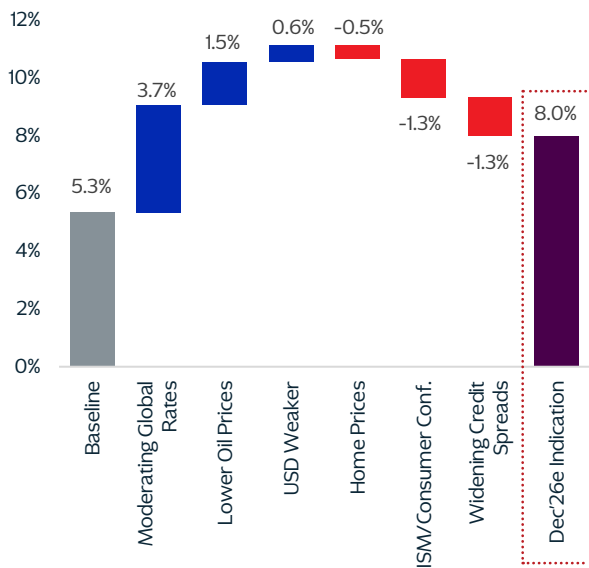
**Dollar vs. Real Rates**



Data as at June 4, 2025. Source: Bloomberg.

**Exhibit 14: Our Earnings Growth Leading Indicator Is Not Calling for Negative Growth Due to Offsetting Positives Like Oil, the USD, and Rates**

**Contributions to December 2026e S&P 500 EPS Growth Leading Indicator**



Our S&P 500 Earnings Growth Leading Indicator ('EGLI') is a combination of seven macro inputs that together we think have significant explanatory power regarding the S&P 500 EPS growth outlook. Data as at July 2, 2025. Source: National Association of Realtors, ISM, Conference Board, Bloomberg, KKR Global Macro & Asset Allocation analysis.

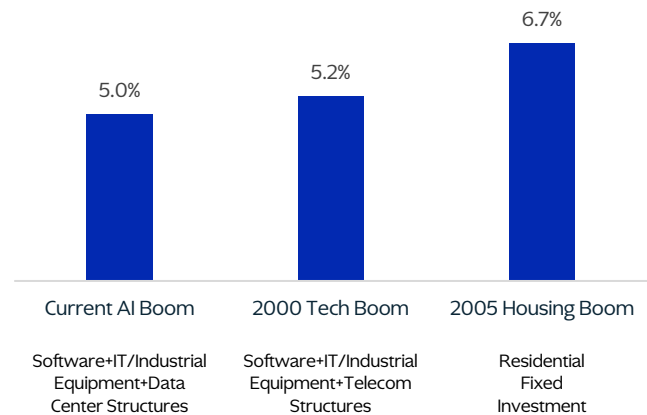
# 3

The speed of change in AI, including the emergence of DeepSeek as well as the capital flowing into this domain, has been even faster than we imagined.

DeepSeek's advancements in artificial intelligence have not only showcased significant technological progress but also underscored China's growing capabilities in the AI sector. Not only is AI reshaping industries, but it is also redefining investment paradigms, as it is creating a complex yet compelling landscape for value creation. Estimates suggest that generative AI revenues could exceed one trillion U.S. dollars annually within the next decade, signaling a significant new market for the tech industry. Importantly, technology-led productivity gains could drive overall U.S. GDP higher by just under 1% annually in 2025-26. Thereafter, in 2027 and beyond, we see U.S. productivity growth accelerating to a longer-term run-rate of 1.5-2.0%, which would be well above the 2010-19 norm of 1.3%.

**Exhibit 15: The Current AI Investment Boom Is Quite Large by Historical Measures**

**Investment Spend as a % of U.S. GDP**



Data as at March 31, 2025. Source: Bloomberg.

## 4

## See below for details, but we have even higher conviction in our major investment themes at KKR.

These include Security of Everything, Capital Heavy to Capital Light, Collateral-based Cash Flows, Productivity/ Worker Retraining, and Intra-Asia Trade. In a world where an investor needs to make his or her own luck, having the tailwind of a major investment theme that is not fully priced in represents a major opportunity, we believe.

So, where do we go from here? Given all the crosscurrents shaping today's macro and market environment, our message is to stay the course. The cycle is not over, many investors are still not fully invested, and there are several mega investment themes that have not yet fully played out. However, we fully acknowledge that the low rate, low volatility beta-trade is now over. To this end, our long-held *Regime Change* top-down framework is gaining further momentum.

If we had one tweak to make as we move into the second half of the year, as far as it relates to our '*Glass Still Half Full*' thesis, it would be to favor the notion of '*Make Your Own Luck*'. In Private Equity, for example, this means owning more control positions where outcomes are driven by operational improvement and/or employee ownership, rather than by leverage or some opportunistic refinancing. In Credit, we find that using relative value as a guiding principle while being disciplined when it comes to portfolio construction, and having the ability to allocate up and down the capital structure and across geographies, can lead to differentiated investment outcomes. All else being equal, we also want to be higher up in the capital structure when we can. In Real Assets, we think that owning contractual cash flows that both protect the downside and provide some upside optionality is warranted.

What would we avoid? While our base view is that markets continue to grind their way higher in 2025, we think highly levered corporate debt deals, low-end consumer spending, and the auto and food sectors remain areas of potential caution. We also want to reduce our

dollar overweight and not be overly long duration in our portfolio construction. Further, we also want to minimize exposure to companies that failed to properly diversify their supply chains during the pandemic. However, embedded in our outlook (which we describe in more detail in Section II) is that we do not experience a sustained global recession, despite some weak growth quarters ahead across the various regions where we invest.

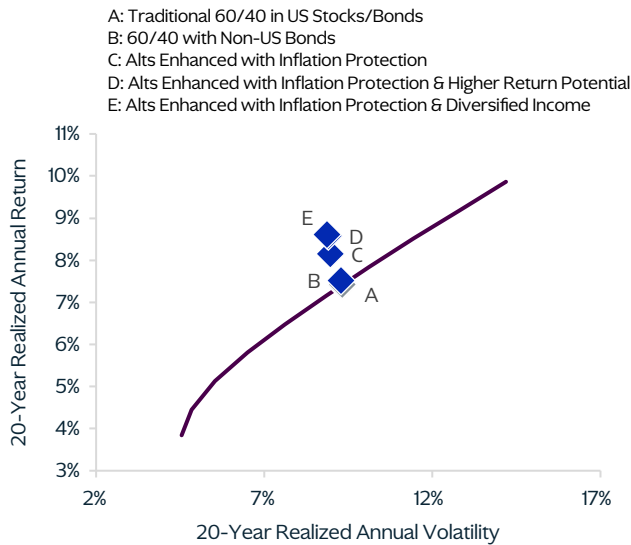
In terms of new asset allocation work, we have updated our Picks and Pans, refreshed our expected return forecasts, and outlined model portfolios we believe are well-positioned to outperform in the current *Regime Change* environment. Our message, similar to what we said at the start of the year, is that we expect a tighter dispersion of returns across asset classes (*Exhibit 10*), underscoring the importance of upfront yield, non-correlation, and alpha generation (e.g., operational improvement). Simply stated, we are moving away from a period of benign globalization that favored beta, duration, and indexing towards one that is centered on 'making our own luck.'

In terms of risks, we see stagflation, higher rates, and a weaker dollar as the potential pitfalls that currently warrant investor attention (See Section III, Capital Markets, for more details.) The other area where we are spending more time is on forecasting the 'right' spending level for AI. As we show in *Exhibit 15*, AI-related spending in the U.S. is already running near 5.0% of GDP—not far from levels seen during the Dot.com boom or at the peak of the housing cycle. Our message is that there will be both winners and losers, given the amount of capital chasing returns in this area of the economy. Finally, there will be many unpredictable geopolitical considerations that are impossible to ignore as we continue the transition from benign globalization towards great power competition.

In Private Equity, for example, this means owning more control positions where outcomes are driven by operational improvement and/or employee ownership.

**Exhibit 16: In a Regime Change, Shifts Away From Government Bonds Towards Alternatives Can Boost Return and Drive More Diversification**

**20-Year Annual Returns and Volatility of Various 60/40 Portfolios, %**

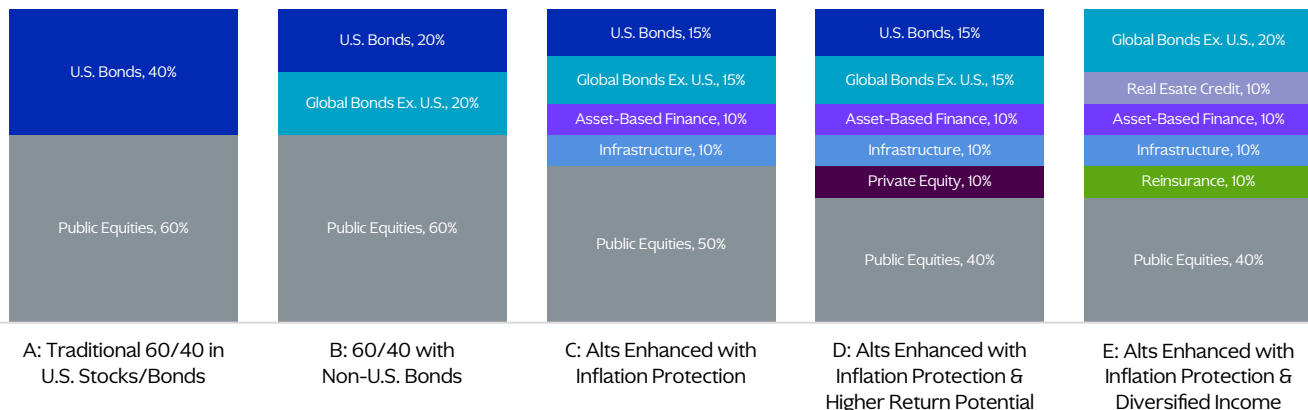


Realized annualized returns are calculated from quarterly returns, and volatilities are calculated using annual total returns from 2004 to 2024 to partially correct for the downward bias for private market proxy volatility. Proxies are defined as follows: U.S. Stocks: S&P 500 Index; U.S. Bonds: U.S. Aggregate; Global Bonds: Global Aggregated Hedged in USD; Infrastructure: Burgiss Infrastructure Index; Private Equity: Cambridge Buyout Index; Asset-Based Finance: KKR Private Credit ABF composite investments post January 1, 2017, backfilled with Burgiss Private Credit Index. Source: Bloomberg, Burgiss, KKR Global Macro & Asset Allocation analysis.

Looking at the big picture, we want to reiterate our view that ‘this time is different’, which is the centerpiece of our long-held *Regime Change* framework. Specifically, we believe that we have moved from a period of low growth, low inflation, tight fiscal, and loose monetary policy, towards one with higher nominal GDP, loose fiscal policy, bigger deficits, and more geopolitical uncertainty. One can see this in *Exhibit 11*. As part of this thesis, we believe that national security interests are now driving economics and capital flows much more than they did in the past. For CIOs, that means moving past the GFC-era playbook of building portfolios that created resiliency to protect against bank deleveraging, to now focus on hedging against a weaker dollar, higher long-rates, and more equity volatility. One can see this in *Exhibits 16* and *17*. To navigate these crosscurrents, we are leaning into themes that help build durability and demonstrate proven staying power, including the Security of Everything, Productivity/ Worker Retraining, and Collateral-Based Cash Flows. These themes not only are resilient in the face of volatility and uncertainty but also serve as actual foils to some of the headwinds we have identified in our *Regime Change* thesis. Therein lies the opportunity set, we believe.

**Exhibit 17: Traditional 60/40 Portfolios Can Be Improved by Owning Less U.S. Government Bonds and More Alternatives in Many Instances, We Believe**

**Traditional 60/40 and 60/40 with Alternatives Portfolios**



Data as at May 15, 2025. Source: Bloomberg, Burgiss, KKR Global Macro & Asset Allocation analysis.



KKR vs. the Consensus: Variant Perception	
Oil prices remain weaker	We remain cautious on oil prices, as the diminishing geopolitical risk premium brings the bearish fundamental backdrop back into focus. Specifically, we expect the oil market to move into larger surpluses over the next six to 12 months, driving WTI oil prices back down to \$60 per barrel on average in the second half of 2025 and 2026.
During government deleveraging cycles driven by big deficits, the currency may be more vulnerable than the long end of the curve	When consumer and corporate debt are declining at the same time, our observation is that investor discomfort with wide deficits tends to be expressed through currency weakness, rather than a big surge in government bond yields. As such, we are more inclined to hedge the USD than the back end of the curve.
Productivity cycles drive markets longer and higher than many think	Our strong belief is that we are in a productivity cycle similar to the 1990s. As such, market selloffs are to be bought, not sold, as the cycle goes on longer. Meanwhile, on the fixed income side, we think higher starting rates mean that credit spreads remain tighter than the consensus now thinks.
Europe will perform better for longer	Valuation differentials between U.S. and European Equities are near historic extremes at a time when the European story may be changing for the better. From our vantage point, we think defense stocks and banks run further, and we think a stronger euro, continued interest in renewables (given such high energy costs), deeper capital markets, and less onerous cross-border restrictions may all work together to make something more structural for investors to get behind than the consensus now thinks.
We think Private Equity will remain a top-performing asset class	Contrary to a popular recent narrative, we do not see secondary PE sales by universities as a harbinger of doom, but rather as a rational response to potential future liquidity needs related to endowment taxation. Private Equity continues to benefit from dispersion and control, allowing investors to lean into operational improvement and accretive M&A activity. Maybe even more importantly, we think PE increasingly offers the most direct route for tapping into a broad universe of high-quality small and midsize companies measured in terms of their margins, stability, and future growth prospects.
Infrastructure: The role of Private Markets in a time of government retrenchment signals a larger than expected opportunity	We think governments across the globe are being challenged simultaneously by historic fiscal constraints, energy transition needs, and geopolitical competition. Private investments have emerged as a critical source of capital across a variety of industries. Just consider the post-pandemic increase in the need for infrastructure, for example, where demand for capital far exceeds what governments can provide to stand up transmission lines, connect data, build supply chain resiliency, and update existing infrastructure.
Changing labor dynamics suggest the unemployment rate stays lower for longer	We are projecting monthly job growth of only 100-110k over the next 18 months, with gains increasingly narrowly concentrated in just a few sectors, including health care and leisure. Importantly, however, this modest payroll backdrop does not imply a significant increase in unemployment rates. In fact, we believe the U.S. may need just 50-100k jobs per month to keep unemployment stable over the long term, as labor force growth slows due to lower immigration and aging demographics.
U.S. markets are reasonably valued, not overvalued	Lower taxes (higher free cash flow), higher margins, and higher quality earnings all suggest the S&P 500 is not at extreme valuations. Even within the Magnificent Seven, companies have negative net debt and high free cash flow conversion.
The technical picture remains much better than investors think	Net issuance of IPOs, Levered Loans, and High Yield remains at levels not seen since 2009. Meanwhile, the Fed's balance sheet still has holdings that are equal to 24% of GDP. To be sure, today's level is below the record of 34% of U.S. GDP reached immediately after COVID, but it remains a far cry from the six percent that defined the pre-GFC era.

## SECTION I

# Key Themes

## Security of Everything

When we wrote *State of Play* in early 2022, shortly after Russia's invasion of Ukraine and with COVID barely behind us, our colleagues within the KKR Global Institute, Vance Serchuk in particular, helped us to better understand how the world might evolve and change in the coming years. At that time, we noted that, from an economic standpoint, the democratization effects of global trade, many of which were envisioned following the creation of the WTO in 1995, were likely to be replaced by 'like-minded blocks' rather than truly integrated, global markets.

This trend has only accelerated under the Trump administration, where governments, businesses, and individuals now better understand that the reliance on past paradigms can come at the expense of resiliency. Indeed, the old paradigms likely cannot work in today's world. Consider global military expenditure hit US\$2.6 trillion in 2024, representing about 2.4% of global GDP—up from roughly 2.2% in 2021-22. So far, this increase has been driven by higher spending in Europe and Asia, but we think it is headed higher around the world. President Trump's emphasis on policies promoting self-reliance (rather than dependence on the U.S.) will spur significantly more efforts to strengthen and rebuild national defense systems.

Indeed, Germany recently announced plans to increase defense spending by 70%, reaching €162 billion by 2029. This rapid expansion is the fastest among the continent's leading economies and signifies a notable shift away from that country's post-Cold War stance. At the same time, Brussels too is setting a new tone with a €150 billion plan to rearm Europe. During the June 2025 NATO and EU gatherings, European leaders agreed on a new defense spending goal—aiming for 5% of GDP to be spent on core defense and military infrastructure (3.5%) as well as cybersecurity or hybrid threats (1.5%)—significantly higher

than the previous 2% commitment. European Council President António Costa highlighted that much of this increased expenditure will go towards U.S.-made military equipment, using it as leverage to push for broader trade agreements and to curb potential U.S. tariffs.

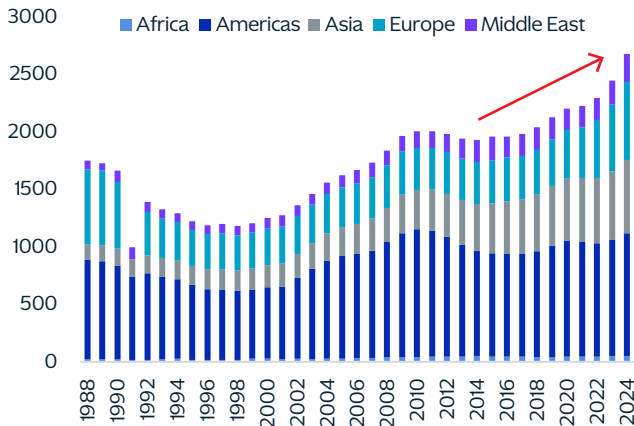
Fiscal policies are also adjusting. The European Commission confirmed its willingness to relax deficit rules, allowing member states to fund rearmament initiatives outside their usual budget constraints. While this facilitates front-loaded defense investments, it also raises questions about sovereign bond issuance in the medium term.

Meanwhile, the Middle East War reinforced the 'weaponization of everything' thesis as the world marveled as beepers, cell phones, and other items were weaponized through their supply chains. As we have discussed over the last several years at KKR, we think the desire for self-sufficiency, security, and resilience across governments and corporations will ultimately reshape energy policies, supply chains, and even consumption patterns. In line with this shift, we believe the definition of 'security' continues to expand beyond traditional military concerns. Governments, corporations, and organizations such as NATO increasingly view security through a broader lens—covering data, transportation, payments, communications, and healthcare—and critically need supply chains for each. It is a reminder that the global landscape is shifting, and the implications for portfolios, policy, and strategic positioning are potentially quite profound, we believe.

Governments, corporations, and organizations such as NATO increasingly view security through a broader lens.

**Exhibit 18:** There Have Been Robust Increases in Defense Spending Across Every Region, a Trend We Expect to Accelerate

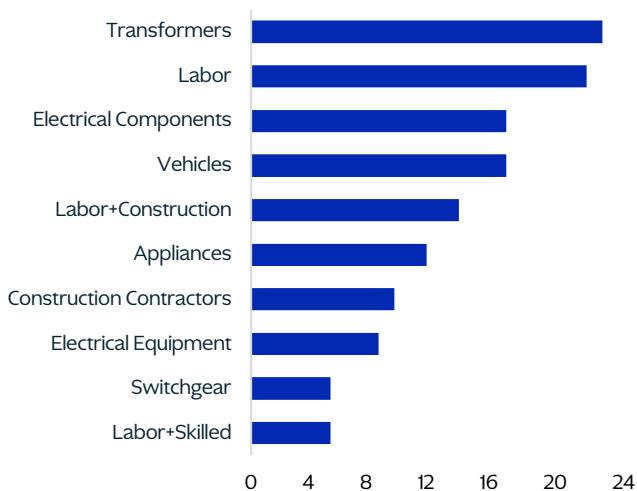
**Military Expenditure by Region, US\$ Billions in 2023  
Prices and Exchange Rates**



For full details and disclosures on calculation refer to <https://www.sipri.org/databases/milex>. Data as at December 31, 2024. Source: Stockholm International Peace Research Institute, Goldman Sachs Research.

**Exhibit 19:** Supply and Demand for Industrial Equipment Are Out of Balance Due to Underinvestment, the Energy Transition, and Weather

**Supply Shortages in ISM Subsectors, Number of Months in the Last 2 Years**



Data as October 31, 2023. Source: U.S. Census Bureau.

## The Loneliness Epidemic, Including Pet Care and Fertility

Social disconnection is increasingly becoming a defining feature of modern life, shaped by demographic shifts and technological disruptions that are transforming societies worldwide. In the aftermath of the pandemic, then U.S. Surgeon General Vivek Murthy declared loneliness a public health crisis, warning of a “fraying of the social fabric” amid long-term declines in social participation and trust. Americans now spend roughly 24 more hours alone each month (and 20 fewer with friends) than they did in 2003. Emotional costs are mounting—nearly three-quarters of Gen Z in the U.S. report feeling lonely, alongside significant shares of adults in Japan, China, and the U.K. Meanwhile, financial pressures and shifting cultural norms are prompting young adults to delay or forgo traditional milestones such as moving out, buying a home, partnering, or having children, which historically anchored identity and social connection. These trends are exacerbated by the retirement and increased longevity of the massive baby boomer generation, which we think will entail more older Americans living alone. As more individuals explore alternative paths to community, new economic opportunities are emerging through digital platforms, pet care, co-living models, and innovative fertility solutions.

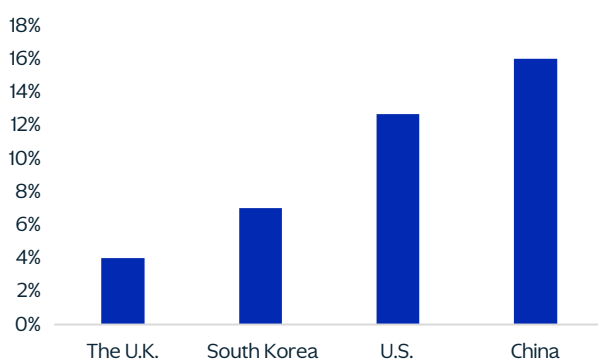
Solitude is evolving into a powerful force reshaping consumer behavior. As our colleague Changchun Hua has highlighted, consumption patterns in East Asia reflect broader demographic and economic realities, and since 2020, trends in Japan—where the median age now sits at 50—look markedly different. Indeed, we are seeing a broader global transition underway: aging populations, urbanization, and the rise of solitary living are driving new and different forms of social engagement. In the U.S., home prices, now near multi-decade highs, have helped push the median age of first-time homeowners from 31 to 39 since 2014, extending the period young adults live with their parents. The decline of partnered households and the doubling of one-person households since 1960—now accounting for 29% in the U.S. and 37% in Japan—is further evidence of shifting social structures.

Despite these trends, connections are taking new forms. In China, where marriage and fertility rates have fully halved over the past decade, the urban pet population is projected to surpass the number of young children in the coming years. This has driven sustained growth in premium pet food and veterinary care, reflecting a broader embrace of pets as companions. Across East Asia, we also observe rising interest in digital wellness platforms and policy initiatives that support co-living spaces and ‘third places’ that foster new types of community. Ultimately, the pursuit of social connection remains fundamental to human nature, but its expression is now less tied to homeownership, marriage, and traditional family structures, and increasingly is individualized and flexible.

Today, only 20% of Americans aged 18 to 29 are married—down from 59% in 1960—and the median age of marriage has advanced by more than seven years over the same period. As these trends accelerate, particularly across East Asia, scalable platforms like dating apps that facilitate personalized connections present significant opportunities for growth. Concurrently, we believe that investment in fertility solutions will become increasingly vital as women delay childbirth. Where these trends persist, digital fertility clinics, pharmaceuticals, genetic testing, and family-planning platforms will, we think, become essential components of a modern, technology-enabled infrastructure supporting new family trajectories.

#### Exhibit 20: We Think the Desire for Companionship—and the Embrace of Pets—Is a Powerful Investing Trend

##### CAGR in Pet Food Sales, 2017-2023, %



Data as at December 31, 2023. Source: Pet Food Industry, Euromonitor, USDA FAS, industry estimates.

## Worker Retraining/Productivity

We think there is a massive economic opportunity to invest in workforce training and/or retraining that prepares workers to fill job openings across manufacturing, logistics, nursing, etc., left open because of baby boomer retirements and/or evolving societal needs. President Trump has also espoused a clear shift from strictly academic pathways towards more vocational and technical education, emphasizing the need for worker training and upskilling to meet the demands of a reindustrialized American economy. Against this backdrop, a rethinking of approach may be warranted. An Executive Order on Workforce Modernization in April 2025 set the stage for a major overhaul of federal workforce programs, aiming to align them with emerging industries and sectors that are shaping the ‘future economy’, especially AI and advanced manufacturing. A key component of this effort is the expansion of initiatives that offer practical, hands-on training, with the goal of supporting over one million new apprenticeships annually aimed at addressing the growing shortage of skilled tradespeople.

The reauthorization of the Perkins Act reinforces this focus, providing over \$1.3 billion annually to states to boost vocational education for more than 13 million individuals. Meanwhile, a proposed budget realignment includes a \$900 million increase in funding for career and technical education (which is actually coupled with cuts to traditional higher education programs). This represents a clear shift in resources towards vocational training, emphasizing skills development over conventional academic pathways.

Overall, these measures reflect a strategic pivot towards building a more adaptable, industry-ready workforce aligned with the demands of a rapidly evolving economic landscape. Areas where we see opportunity could include: 1) shifting job requirements from a credentials-first model to a skills-first model that can optimize ROI in education and training and also lead to more employable people; 2) building on the above skills-first approach, emphasizing ‘skills adjacency’ strategies for existing workers that can facilitate upskilling where jobs have some overlap with, or even all of, the skills needed for new roles; 3) certifications to confirm training in areas of specific national need

and employment relevance; and 4) expansion of hybrid platform models that provide online credentialing paired with personalized coaching.

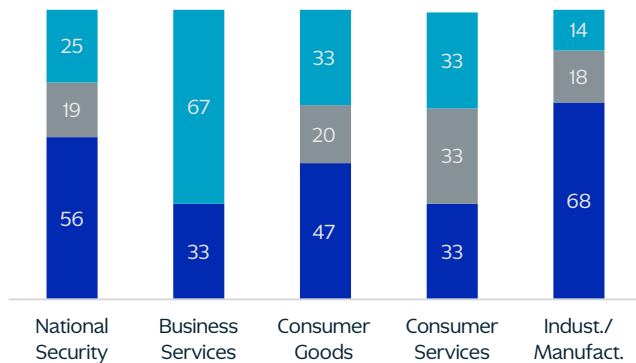
Against a backdrop of enhanced skills requirements and stickier wages, we think strong productivity will be needed to allow corporate margins to hold. Morgan Stanley estimates that net immigration will decline from a peak of 3.3 million in 2023 and approximately 2.8 million in 2024, to around 1.0 million in 2025, and 0.5 million in 2026. We agree.

So, going forward, we see investment opportunities in areas such as labor market analytics, job search tools, skills-based training (on- and off-line), and productivity ‘enhancers,’ including workflow tools and automation. AI will only accelerate the need for retraining, we believe. Against this backdrop, Brian Leung is now projecting productivity in the U.S. in the 1-2% range longer term, a critical estimate that is supported by robust new business formation, technology investment, and worker retraining/reskilling.

**Exhibit 21: Qualified Labor Is a Major Challenge for Manufacturing, Consumer Goods, and National Security**

**Availability of Qualified Labor a Major Consideration for Your Companies as They Consider Producing More Goods in the U.S.? (% Share of Respondents)**

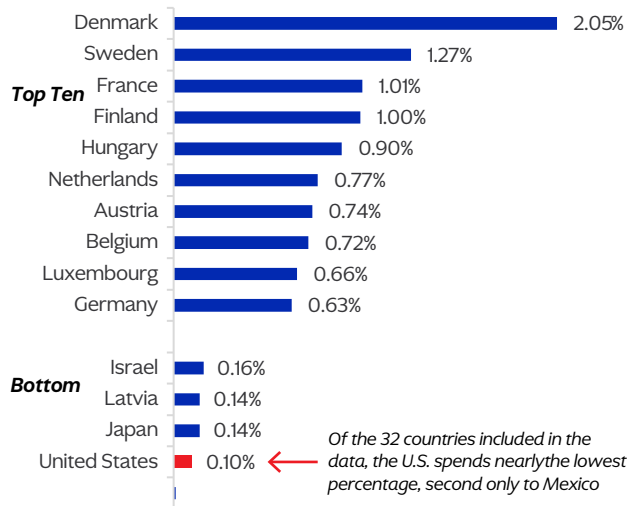
■ Yes, a Major Concern ■ Yes, Training Programs Could Help ■ No



Responses are expressed as share of respondents. Data as at May 31, 2025. Source: BofA Global Research.

**Exhibit 22: The U.S. Spends Less On Worker Retraining Than 31 Out of 32 OECD Countries Studied**

**Public Expenditures on Assistance and Retraining for Unemployed Workers in Top Developed Economies as a % of GDP**



Data as at December 31, 2022. Source: U.S. Department of Commerce.

**Public to Private Initiatives**

We’re witnessing a profound transformation in the capital formation landscape—one where private capital is increasingly stepping into roles once dominated by governments, many of whom are now over-levered. Across the globe, public balance sheets are stretched thin by rising debt burdens, aging populations, and a growing backlog of societal obligations. In this environment, policymakers face tough trade-offs, and the emerging reality is clear: Private investors are becoming essential to funding everything from infrastructure and housing to energy transition and strategic corporate ownership. As part of this transition, sovereigns are increasingly leveraging Private Markets to deploy excess revenues more efficiently, diversify away from single-resource dependencies, and secure strategic stakes in critical sectors of their economies.

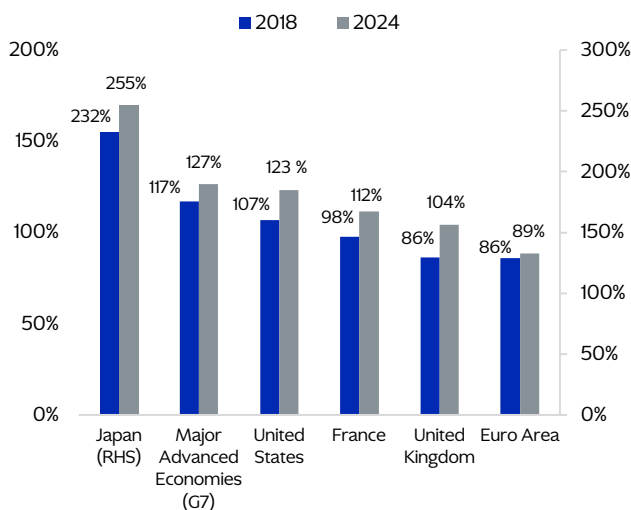
Meanwhile, the retreat of traditional lenders, coupled with a surge in private company formation, is reshaping the capital stack. The Private Markets are not only expanding; they are also deepening, with broader institutional



participation and increasingly segmented specialization. We believe this acceleration is only getting started. So, whether it is stabilizing real estate markets, recapitalizing sectors in deleveraging mode, or funding long-term infrastructure projects like energy transmission and digital connectivity, private capital is now a core part of the solution set. This is not solely about yield; it is about solving real-world problems that public capital can no longer address at scale—building resilient supply chains, ensuring retirement security, accelerating the energy transition, and maintaining competitiveness amid geopolitical fragmentation. For investors, that means a deeper understanding of how each private asset class can serve both return and impact, driving stability in an uncertain world. In our view, the handoff from government to private capital is one of the defining themes of this regime. Those who understand its nuances—and position accordingly—will be best placed to generate durable alpha over the coming years. That said, it also requires shareholders to understand, navigate, and engage with the stakeholders impacted by the assets or businesses they fund.

**Exhibit 23: Governments in the Developed World Are Now More Levered, Which Likely Means That the Private Sector Will Need to Fund Growth in Key Asset Classes Such as Infrastructure**

**Advanced Economies Government Debt, as a % of GDP**



Data as at May 31, 2025. Source: Bloomberg.

**Exhibit 24: \$3.7 Trillion Per Year of Investment in Economic Infrastructure Is Needed to 2035 to Keep Pace With Expected GDP Growth**

Global Average Infrastructure Need, % of GDP and US\$ Trillions		
	% of Global GDP per Annum	US\$ Trillions Spend in Aggregate, 2017-2035
Roads	1.0%	18.0
Rail	0.4%	7.9
Ports	0.1%	1.6
Airports	0.1%	2.1
Power	1.3%	20.2
Water	0.5%	9.1
Telecom	0.6%	10.4
<b>Total</b>	<b>4.1%</b>	<b>69.4</b>

Data as at December 31, 2017. Source: IHS Global Insight, ITF, GWI, National Statistics, McKinsey Global Institute analysis.

## Models Transitioning to Capital Light From Capital Heavy

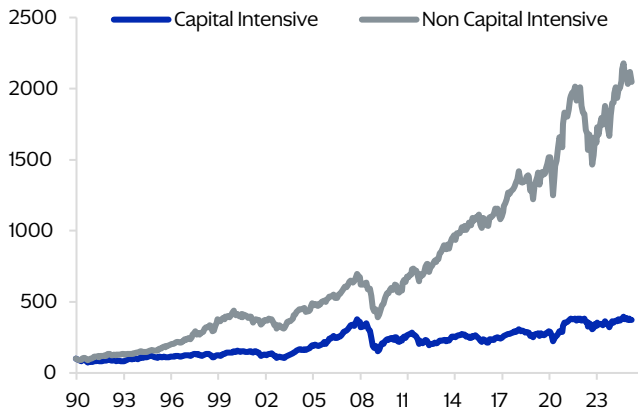
A growing number of public companies are effectively transitioning towards private-like models, not through LBOs, but via disciplined capital allocation. Buybacks remain a primary lever, with the S&P 500 repurchasing nearly \$5 trillion of stock over the past six years, and Europe showing a similar pattern—around €1 trillion in the same period, with a 46% increase in 2024 alone. Importantly, many of these firms are funding buybacks through divestitures of capital-intensive assets, including securitizations and non-core unit sales. This recycling of capital is reshaping corporate balance sheets and capital structures. We see this trend as supporting EPS growth and uncovering opportunities to invest in listed companies with clear pathways towards more focused, capital-efficient operations.

Simultaneously, there is an acceleration in companies strategically repositioning around capital light models, deliberately reducing exposure to cyclical businesses to improve visibility on earnings, margins, and returns. This structural shift creates actionable opportunities, both in acquiring equity stakes in these transitioning businesses and in directly purchasing carved-out assets. In our view, corporate carve-outs stand out as some of the most attractive sourcing channels in today's bifurcated markets, where complexity is often undervalued or misunderstood.

Across our 24 offices globally, we continue to identify outsized opportunities in sectors like Private Equity, Infrastructure, and Energy. In large markets such as the U.S. and Japan, we would not be surprised if carve-outs account for a third or more of total deal flow over the next 12 to 24 months. These transactions often come at more attractive entry prices than traditional private deals and tend to offer significant operational upside.

**Exhibit 25: Non-Capital-Intensive Companies Are Breaking Out. We Like Both the Equity Being Converted Towards Capital Light As Well As the Financing of the Assets Being Sold**

**World Capital vs. Non-Capital Intensive, USD Price Return Indexed to 100 in January 1990**



Capital intensity based on: Assets/Employee, Asset/Net Income, and Capex/Net Income. Data as at March 31, 2025. Source: Goldman Sachs.

## Collateral-Based Cash Flows

Our research continues to show that many individual and institutional investors are still underweight Real Assets, especially Infrastructure, Asset-Based Finance, Real Estate Credit, and certain parts of Energy, during a time when the need for inflation protection in portfolios remains high. These products also have a degree of inflation linkage, given they are 1) either backed by hard assets that tend to rise in value with consumer prices and often have floating coupons that may benefit lenders during periods of rising rates (e.g., Asset-Based Finance), or 2) they have pricing escalators/contracted revenues that are longer-term in nature.

While most investors are focused on the semiconductor angle of the current AI boom, we have been spending more time studying the energy demand surge needed to power these models. The reality is, in many instances, existing infrastructure is insufficient to meet the demand required. Against this backdrop, we are bullish on critical energy transmission assets, data centers, and cooling technologies.

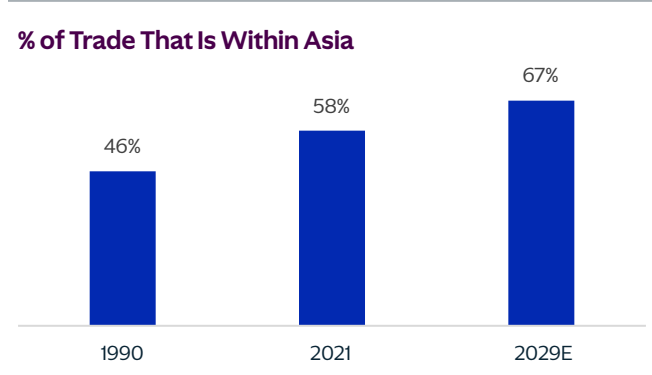
Meanwhile, we heavily favor Asset-Based Finance as a play on our *Regime Change* thesis within the Credit markets. The market opportunity is significant, as lending in this asset class now approaches \$6 trillion today and is projected to surpass \$9 trillion, which is multiples the size of High Yield, Levered Loans, and/or Direct Lending. We think the spread to other forms of Credit in terms of potential absolute return in the Asset-Based Finance market now appears quite compelling. Even with inflation cooling and the Fed embarking on an easing campaign, we still think ‘higher for longer’ will remain in play.

## Intra-Asia Connectivity

Intra-Asia trade—which we see as a mega theme—continues to accelerate and in our view, remains one of the true structural investing stories in the region as the economic landscape is reshaped. As supply chains decouple from traditional Western dependencies and regional demand ramps up, intra-Asia flows are increasingly becoming localized. Governments across Asia are prioritizing trade facilitation and infrastructure connectivity to anchor this shift and drive sustained intra-regional growth. Back in 1990, only 46% of Asian trade was conducted within the region; by 2021, that percentage had risen to 58%, and we expect it to grow another 10% over the coming years. While this growth is accompanied by rising rivalries among countries, China has managed to increase its share not just through competitive exports but also by establishing a stronger local presence in key markets like Vietnam. One of the emerging benefits for the region involves the increasing frequency of countries transacting in renminbi, a trend that has gained momentum post-COVID. For us at KKR, this is a scalable, secular trend with real investment potential that spans logistics, manufacturing, consumer markets, and digital enablement. We think Infrastructure and Credit—both

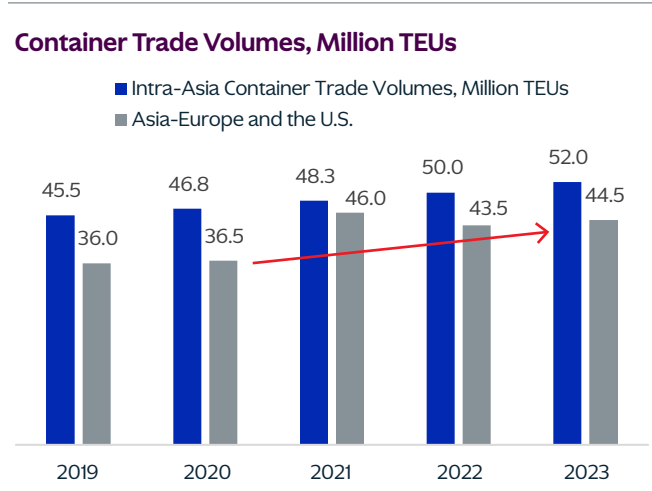
liquid and private—also offer compelling ways to capitalize on this ongoing regional shift.

**Exhibit 26:** In 1990, Just 46% of Asian Trade Took Place Within Asia; By 2021, That Figure Had Reached 58%



Data as at December 31, 2023. Source: The Economist.

**Exhibit 27:** For Every 7 Containers Shipped to the U.S. and Europe, Another 8 Are Shipped Within the Far East



Data as at December 31, 2023. Source: Xeneta.

From a macro perspective, India’s relative insulation from global trade friction remains intact, supported by its predominantly domestic, consumer-driven economy.

# Picks and Pans

## ▲ India (NEW)

We continue to see India as one of the most compelling strategic allocations within emerging markets today. From a macro perspective, India’s relative insulation from global trade friction remains intact, supported by its predominantly domestic, consumer-driven economy and a services-focused export sector that is less vulnerable to tariffs. As the global trade landscape recalibrates, India is well-positioned to increase its manufacturing share, particularly as oil prices soften and ‘China+1’ strategies become more entrenched. Cyclically, we are observing early signs of a rebound following a soft patch in 2024, driven by rural income recovery, robust services exports, and, importantly, supportive policy measures. Production-linked incentives and eased FDI rules are central to government efforts to attract broader capital inflows. The Reserve Bank of India’s rate cuts and the recent fiscal year budget, which injects meaningful stimulus for low- and middle-income households, further bolster this outlook. Structurally, India presents a unique combination: strong nominal GDP growth, declining real interest rates, expanding domestic capital markets, and a long-term consumer runway unmatched in many other markets. For investors, India also offers diversification benefits. Its equity market correlation with global indices has decreased—and the sheer scale of its economy is expected to unlock significant private sector opportunities over the next decade. While we anticipate a modest depreciation of the rupee, this can be hedged, and the core investment thesis remains compelling: in a volatile global environment, India’s stability, ongoing reforms, and resilient consumer base create a differentiated and increasingly scalable opportunity.

## ▲ Japan Intercompany Holdings (REPEAT)

No doubt, there are many compelling investment ideas beyond corporate carve-outs and public-to-privates in Japan. One where we are particularly focused involves

the accelerating unwind of Japanese strategic holdings within the corporate sector, a backdrop that is encouraging a wave of stock buybacks from the likes of Sony, Toyota, Uniqlo, and Mitsubishi. This activity aligns with the Tokyo Stock Exchange's push to encourage major companies to dismantle their cross-shareholdings that were historically used to strengthen business relationships but are now often viewed as a barrier to effective oversight and shareholder accountability. As Japan's focus on enhancing shareholder returns intensifies, many of these mutual holdings are being unwound, enabling companies to buy back shares at generally accretive levels. Additionally, Japan's Financial Services Agency has introduced new disclosure guidelines, making it more difficult for firms to reclassify strategic holdings as purely investment-driven. This has increased scrutiny on hesitant shareholders, further accelerating the unwinding process. So, we continue to view the ongoing unwinding of these holdings as positive in that they are creating a virtuous cycle by unlocking dormant capital, enabling sellers to prioritize growth initiatives, while providing buyers with improved opportunities to enhance return on equity. This trend represents a meaningful shift in Japan's corporate landscape, with potentially favorable implications for investors.

## ▲ CLO BB Liabilities (NEW)

We are constructive on shorter duration CLO BB liabilities as a high-carry, risk-adjusted opportunity in today's credit landscape. In our view, CLO BBs offer compensated complexity as investors are getting paid to take structured credit risks in a part of the capital stack that was fundamentally de-risked post-GFC. From a structural perspective, CLO BB tranches benefit from significant subordination and diversification, supported by active collateral management and tested legal frameworks. These securities sit above equity and equity-like risk but still offer double-digit yields. That combination—credit enhancement plus meaningful income—is increasingly rare in a market where yield has been repriced, but not all risks are being equally rewarded. Importantly, we are seeing CLO BBs as dislocated relative to both their fundamentals and historical spread behavior. However, spreads remain wide due to technical pressures such as regulatory constraints, retail outflows, and risk aversion, not a

material degradation in underlying loan performance. Defaults remain manageable, recoveries have been higher than feared by some, and most importantly, the CLO market continues to prove its resilience in periods of volatility—especially for seasoned vintages with shorter duration.

## ▲ Asia Real Estate (NEW)

We view Asia Real Estate as a high-conviction investment idea where structural growth and market dislocation converge. While sentiment has been clouded by headlines out of China, we see opportunities emerging in markets like Japan, India, and Southeast Asia, where real estate cycles are either early or just starting to turn. Even in China, we believe that the housing correction is beginning to turn the corner. Where do we see opportunities? In our view, logistics, multifamily, and digital infrastructure are especially compelling. The long-term drivers—urbanization, digitalization, and middle-class expansion—remain firmly intact. At the same time, global institutions are underweight Asia Real Estate relative to its contribution to global GDP. As asset allocators reassess exposure and look for diversification away from the U.S. and Europe, we think Asia becomes a natural destination—especially in markets with policy tailwinds, favorable demographics, and proven local partners in certain key markets.

## ▲ FX Volatility, Not Rate Volatility (NEW)

We currently favor FX volatility over rate volatility as a more efficient and differentiated expression of macro risk. In a world where central banks are increasingly synchronized and intervention-heavy, rate volatility has become more policy-suppressed—less predictive, less directional, and often less rewarding. FX vol, by contrast, is freer to reflect macro dispersion: fiscal divergence, balance-of-payment shifts, and geopolitical asymmetries. In many ways, FX is the release valve for our current 'Regime Change' environment, particularly as the dollar's dominance is tested by structural deficits and capital rotation. Positioning in FX allows investors to express relative views across regions, exploit valuation mismatches, and hedge against tail risks, without taking

duration exposure in a volatile rate environment. Further, we think FX volatility offers more clarity, cross-asset correlation, and convexity in a macro landscape defined by uncertainty.

## ▲ Unloved Parts of the Market (NEW)

In a bifurcated market where capital crowds into simplicity, we think the real alpha lies in complexity. That means allocating to sectors that are out of favor but improving on the margin, where we can drive value through repositioning, restructuring, or platform growth. In an environment defined by higher volatility, tighter liquidity, and sharper narrative swings, we believe markets are increasingly prone to mispricing complexity and over-discounting cyclicalities. This creates opportunities for patient capital with operational edge. Take solar panels, for example. Sentiment has soured after years of supply chain disruption, margin compression, and policy uncertainty. However, underneath the noise, the structural demand case is intact—decarbonization, distributed energy, and industrial electrification all require scalable solar infrastructure. We see similar disconnects in select housing adjacencies, consumer staples in emerging markets, Chinese liquid markets, and in segments of health care delivery where utilization is recovering but valuations still reflect COVID overhangs. We also think there is a compelling supply/demand imbalance in structured-equity products, especially for securities that neither fall neatly into an ‘equity’ or ‘debt’ bucket. Importantly, this ‘call to arms’ is not about bottom fishing with bad companies. Rather, it is a call on dispersion increasing during periods of volatility, especially when government policy is miscommunicated and/or technical forces such as hedge fund deleveraging are creating compelling entry points.

## ▲ Emerging Market Local Currency Debt (NEW)

We think emerging market local currency debt is poised for resurgence after over a decade of underperformance. Key to this thesis is our expectation that returns in U.S. assets will be lower going forward, encouraging global allocators to rotate toward other geographies in search

of yield and diversification. Consider that over the past decade, foreign investors—particularly in Europe and Japan—have built substantial exposure to U.S. assets, earning outsized returns and supporting dollar strength. Since 2000, foreign ownership of U.S. Public Equities has more than doubled, and exposure to Treasury duration has notched up consistently in the past decade. Today, however, portfolios overweight the U.S. must contend with higher stock-bond correlation, low compensation for equity risk, and greater idiosyncratic risk. Moreover, we estimate that the U.S. dollar is near 15% above fair value. As these challenges weigh on capital inflows to U.S. assets, EMs stand to benefit.

We like EM local currency debt, which capitalizes on better relative value dynamics for lenders and adds targeted portfolio insulation without compromising on yield. Year-to-date, sovereign borrowers have benefited from a weakening U.S. dollar, which eases the cost burden of servicing dollar-denominated debt. Taken with our view that the dollar has peaked for this cycle, this creates a favorable backdrop for overall fiscal stability. We also note that stronger fundamentals are manifesting in tighter CDS spreads for EM sovereign debt, which contrasts with elevated spreads on U.S. Treasuries. Similarly, we see relative value in EM corporate bonds given historically low default rates and rebounding profitability. Taken together, EM local currency debt offers an opportunity for U.S.-centric portfolios to navigate current challenges without stretching for risk. At a country level, real rates are highest in India, Indonesia, and the Philippines.

## ▼ Cuspy Credit and Non-Control Positions in Equities (REPEAT)

We remain in an environment where slower nominal growth limits pressure on bond yields and helps to encourage more capital markets activity. However, there are likely still too many weak companies with shaky capital structures. Tariffs too will be an unfavorable headwind. We continue to stress the importance of not stretching on the quality front in 2025. In our view, the incremental yield pick-up in the lowest-rated unsecured High Yield, for example, is just not worth it. Against this backdrop,



we think the difference between control and non-control positions will magnify materially in 2025, as demanding equity multiples require greater focus on operational improvement and the ability to retool companies' capital structures, even as borrowing markets thaw.

## ▼ Overly Levered Companies (NEW)

We believe in staying disciplined around avoiding companies with excessive leverage, especially those that are approaching maturity walls or rely on refinancing to sustain their capital structure. The reality is that the many capital structures that were underwritten during and immediately after COVID did not incorporate a 3-4% neutral rate. So, as credit spreads normalize and risk-free rates stay elevated, these borrowers face both cost and availability headwinds at a time when their free cash flow has been compromised. In this cycle, balance sheet strength isn't just a defensive attribute—it's a prerequisite. We think it is important to focus on being long operational leverage, not financial leverage.

## ▼ U.S. Dollar (NEW)

We remain more cautious on the U.S. dollar than many of our peers, particularly as its long-standing tailwinds—rate differentials, capital inflows, and reserve status—face renewed scrutiny. In general, we believe the combination of large and persistent fiscal and current account deficits, shifting geopolitical alliances, and a cautious Fed introduces real asymmetry. According to our models, the USD is around +15% rich relative to its theoretical fair value, making it at the third most expensive level since the 1980s. In this context, we think a change in the trading level of the U.S. dollar is warranted and necessary for U.S. competitiveness. We think this U.S. strength could become a source of volatility, particularly if markets begin to reprice term premium or question the sustainability of U.S. fiscal policy. For us, that means being more intentional with FX exposure, incorporating active hedging strategies, and allocating to geographies where currency risk is a source of potential upside—not unrecognized downside.

Across the globe, public balance sheets are stretched thin by rising debt burdens, aging populations, and a growing backlog of societal obligations. In this environment, policymakers face tough trade-offs, and the emerging reality is clear: Private investors are becoming essential to funding everything from infrastructure and housing to energy transition and strategic corporate ownership.

## SECTION II

# Global / Regional Economic Forecasts

As we detail below in *Exhibit 30*, we are still seeing positive economic momentum across all the major regions where KKR does business. However, when our team thinks about the speed and durability of that growth, trade tensions are clearly front and center. While we expect the tariff negotiations to remain fluid, one thing is clear: tariffs have evolved. Specifically, what were once seen as temporary negotiating tactics are now becoming embedded features of industrial and geopolitical strategy. We are quite certain that this is no longer the tariff cycle of 2018-2019. Today, tariff regimes are broader, more persistent, and are being used as much to steer capital and assert leverage as to protect domestic producers. This is not unique to President Trump, as the Biden Administration maintained many Trump 1.0 tariffs.

Overall, we are now using a base case where the average effective tariff rate (ETR) applied to U.S. imports settles around 17%. We expect our base case will continue to move around as negotiations play out but feel more confident that long-term outcomes seem banded around a range between the mid-teens and low twenties (*Exhibit 28*). Importantly, this band of outcomes remains below the initial ‘Liberation Day’ average rate of 26%.

While our overall ETR forecasts have only increased marginally since our last update, the composition of the tariffs, as well as the implementation strategy, have changed. At the country level, we do believe the courts may ultimately rule as unlawful the current strategy of implementing tariffs under IEEPA authority. Regardless, the administration would still have access to a variety of alternative legal statutes to achieve similar objectives. Looking at the details, we continue to expect that a

relatively high universal ‘baseline’ will remain a critical part of the administration’s tariff framework. Meanwhile, our base case embeds that China’s base tariff rate will remain around 30%. For the EU, we are penciling in a ‘reciprocal rate’ of 15%—though news of recent progress in EU negotiations does seem to offer some potential for a lower number. Finally, in accordance with the recent trade announcement on Vietnam, we are now expecting that several countries in Southeast Asia will face baseline tariffs of 20% and punitive tariffs on transshipments (up to 40%), as the administration cracks down on trade re-routing.

At the product level, we expect ongoing Section 232 investigations to conclude with steel, aluminum, and copper tariffs at 50%, and other strategic goods (e.g., semiconductors, aircraft) generally at 25%. Importantly, our base case does not yet reflect the very high (200%) potential tariffs that President Trump has previewed on pharmaceuticals, given that he has also signaled that these tariffs may not go into effect for some time (i.e., our base case focuses on where we expect tariffs to be in coming quarters, rather than over the very long term). Separately, while we generally expect that sector tariffs will apply broadly, we do assume that there are some country-level exemptions—like what we have already seen with the U.K. trade deal, which included auto exemptions. Overall, our base case embeds that exemptions could bring 232 sector tariffs down to 10% for roughly one-third of relevant imports.

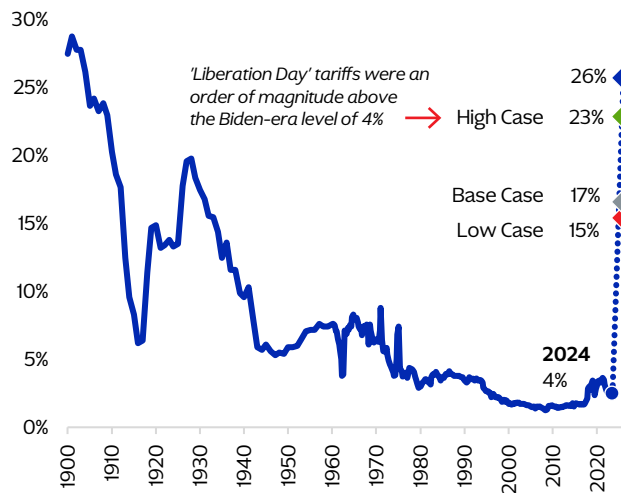
Importantly, tariffs are also just one tool investors must follow in understanding trade policy. Export controls, outbound investment restrictions via expanded CFIUS, and other policies are already in place (many of which were expanded or begun under the Biden Administration) as part of a broader effort by the U.S. government to address national security concerns.

Another area we are continuing to watch closely is the relative importance of goods vs. services to the U.S. economy. As we have previously discussed, our estimates suggest that the gross profitability of U.S. services exports currently surpasses the ‘lost profits’ on goods that the U.S. imports instead of manufacturing domestically.

Overall, the new framework implies a more durable, less volatile tariff regime, reinforcing our view that tariffs are now a structural component of U.S. trade and industrial policy. The investment implications are significant—supporting themes around onshoring, real asset deployment, tariff-insulated supply chains, and portfolio de-risking away from globally-exposed sectors.

**Exhibit 28: Our Base Case Is That Tariffs Settle Around a 17% Weighted Average Rate, Despite All of the Moving Parts**

**U.S. Effective Tariff Rate, %**



Data as at July 9, 2025. Source: U.S. Census Bureau, Goldman Sachs Research, Haver Analytics, KKR Global Macro & Asset Allocation analysis.

**Exhibit 29: Our Tariff Scenarios Reflect an Array of Potential Moving Parts**

**KKR GMAA U.S. Effective Tariff Rate Scenarios by Region and Sector**

Category	Low Case	Base Case	High Case
Europe	10%	15%	15%
Japan/Korea	10%	10%	15%
Southeast Asia	20%	20%	20%
Copper	50% carved out through deals	No deals	No deals
Steel & Aluminum	50% carved out through deals	10% carved out through deals	10% carved out through deals
Other Critical Imports	25% (50% negotiated down to 10%)	25% (33% negotiated down to 10%)	25% (5% negotiated down to 10%)
Autos	50% negotiated down to 10%	50% negotiated down to 10%	10% negotiated down to 10%
Reciprocal Tariffs	Top 10 trading partners	Top 10 trading partners	All trading partners
BRICS 10% Tariff	NA	NA	10% to BRICS+

Transshipping across the board assumption: For SE Asia, we assume that 16.5% of exports from all these countries (\$247 billion worth of imports) are transshipments that end up getting tariffed at a punitive rate.

Scenarios reflect our post-bargaining expectations for tariffs in place in mid-2026 (one year forward). Our scenarios do not reflect the potentially outsized (200%) tariffs that President Trump has threatened on Pharmaceuticals, as he has suggested that these tariffs would not go into place for more than a year. For SE Asia, we assume that 16.5% of exports from Malaysia, Indonesia, Vietnam, Philippines, Bangladesh, Myanmar representing \$247bn worth of imports are transshipments that end up getting tariffed at a punitive 40% rate which pushes the ETR for these countries up to 23.3%. Critical Imports includes Batteries, Lumber, Semis, Pharma. Data as at July 9, 2025. Source: U.S. Census Bureau, Goldman Sachs Research, Haver Analytics, KKR Global Macro & Asset Allocation analysis.

### Exhibit 30: We Are Generally In-Line or Above Consensus on Growth, But We Do Have Concerns About Inflation in 2026

#### KKR GMAA Real GDP and Inflation Forecasts, %

	2025e Real GDP Growth		2025e Inflation		2026e Real GDP Growth		2026e Inflation	
	GMAA	Bloomberg	GMAA	Bloomberg	GMAA	Bloomberg	GMAA	Bloomberg
	New	Consensus	New	Consensus	New	Consensus	New	Consensus
U.S.	1.5-2.0%	1.4%	2.7%	3.0%	1.6%	1.5%	2.9%	2.8%
Euro Area	0.9%	0.9%	1.9%	2.0%	1.3%	1.1%	2.0%	1.9%
China	4.7%	4.5%	0.3%	0.3%	4.1%	4.1%	0.7%	1.0%
Japan	0.7%	0.8%	2.7%	2.8%	0.8%	0.9%	1.8%	1.8%

Data as at June 15, 2025. Source: Bloomberg, KKR Global Macro & Asset Allocation analysis.

## U.S. GDP

**Forecast:** We have modestly revised up our U.S. GDP forecasts for 2025 and 2026, reflecting a slightly more accommodative tax policy (spurred mainly by inclusion in the ‘Big Beautiful Bill’ of President Trump’s promises around taxation of tips and overtime) and slightly milder spending restraint by the U.S. government than previously anticipated (*Exhibits 32 and 33*). Specifically, our updated base case now calls for 1.5-2.0% real growth in 2025 (vs. 1.0-2.0% previously) and 1.6% in 2026 (vs. 1.3% previously). While still subdued in outright terms, our updated growth forecasts are above consensus (1.4% and 1.5% this year and next, respectively), which we think has yet to fully embed the more generous elements of the reconciliation bill, or the marginally more settled tariff backdrop.

Labor dynamics also reinforce our view of a constrained growth environment. We are projecting monthly job growth of only 100-110k over the next 18 months, with gains increasingly narrowly concentrated in just a few sectors, including health care and leisure.

### Exhibit 31: Our Forecasts Remain a Mixed Bag

#### KKR GMAA Real GDP and Inflation Forecasts, %

	KKR GMAA Real GDP Forecast and Probability, %			KKR GMAA Inflation Forecast and Probability, %		
	Base	Low	High	Base	Low	High
<b>U.S.</b>	<b>50%</b>	<b>35%</b>	<b>15%</b>	<b>50%</b>	<b>35%</b>	<b>15%</b>
2025e	1.5-2.0%	1.25%	2.5%	2.7%	2.4%	3.3%
2026e	1.6%	-0.5%	2.5%	2.9%	2.0%	4.0%
<b>Euro Area</b>	<b>60%</b>	<b>20%</b>	<b>20%</b>	<b>60%</b>	<b>20%</b>	<b>20%</b>
2025e	0.9%	0.4%	1.8%	1.9%	1.3%	2.7%
2026e	1.3%	0.7%	1.6%	2.0%	1.6%	2.5%
<b>China</b>	<b>55%</b>	<b>30%</b>	<b>15%</b>	<b>55%</b>	<b>30%</b>	<b>15%</b>
2025e	4.7%	4.4%	5.0%	0.3%	-0.1%	0.7%
2026e	4.1%	3.6%	4.6%	0.7%	0.2%	1.2%
<b>Japan</b>	<b>60%</b>	<b>20%</b>	<b>20%</b>	<b>60%</b>	<b>20%</b>	<b>20%</b>
2025e	0.7%	0.3%	1.1%	2.7%	2.2%	3.2%
2026e	0.8%	0.4%	1.2%	1.8%	1.3%	2.3%

In the U.S. for 2025 and 2026, we assign a probability of 50% for the base case, 35% for the bear case, and 15% for the bull case. In China for 2025 and 2026, we assign a probability of 55% for the base case, 30% for the low case, and 15% for the high case. In Europe and Japan for 2025 and 2026, we assign a probability of 60% for the base case, 20% for the low case, and 20% for the high case. Data as at June 15, 2025. Source: KKR Global Macro & Asset Allocation analysis.

**Commentary:** From an investing standpoint, it’s crucial to frame our growth forecasts within a broader structural context. Tariffs have become a key input in our models—a permanent supply-side shock that we view as being on par with a one-time jump in oil prices to approximately \$125 per barrel. We are modeling an average tariff rate settling around 17%, which will continue to pressure goods inflation, squeeze corporate margins, and influence capital allocation across tradable sectors.

Labor dynamics also reinforce our view of a constrained growth environment. We are projecting monthly job

growth of only 100-110k over the next 18 months, with gains increasingly narrowly concentrated in just a few sectors, including health care and leisure. Importantly, however, this modest payroll backdrop does not imply a significant increase in unemployment rates. In fact, we believe the U.S. may need just 50-100k jobs per month to keep unemployment stable over the long term, as labor force growth slows due to lower immigration and aging demographics.

Productivity, a key swing factor in our outlook, is expected to dip below 1% in 2025-26 before gradually returning to the 1-2% range over the medium term. Importantly, we see this slowdown as cyclical, not structural, supported by ongoing strength in business formation, tech investment, and gains in sectors like TMT, professional services, and energy.

Meanwhile, U.S. consumers are proceeding cautiously. Deleveraging is evident across mortgages, auto loans, and credit cards, and discretionary spending on big-ticket items is softening. Nonetheless, household balance sheets remain generally healthy, and we expect employment and income trends to stay stable enough to keep delinquencies in check and maintain core demand.

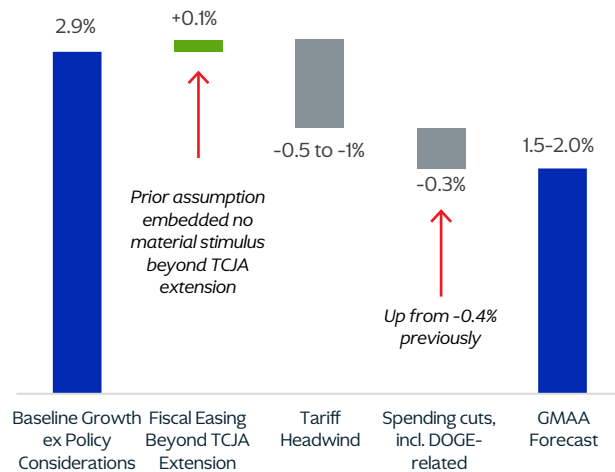
On the fiscal front, the story is also more nuanced. While headline deficits look large (averaging 6.4% of GDP through 2029), our detailed analysis suggests they are less expansionary than they appear. Much of the spending is extensions of existing policies (like the TCJA tax cuts). Meanwhile, revenues from tariffs—roughly \$280 billion annually—provide a meaningful offset. In short, we do not see deficits ballooning from here, nor do we anticipate them crowding out private investment more than they have already.

From an investment perspective, deficits should be viewed as a structural factor, not merely cyclical. They are fostering a regime marked by higher nominal GDP growth, more active industrial policies, and a reduced role for monetary dominance. This evolving environment challenges traditional asset allocation models. Investors need to factor in deficits as key drivers of term premiums, inflation volatility, and currency movements. The strategic advice: focus on assets with contractual cash flows, collateral backing, and alignment with policy shifts—such as Infrastructure, Asset-Based Finance, and Private Credit—and exercise caution with long-duration exposures

that rely on a quick return to disinflation and fiscal restraint. In this context, fiscal policy isn't just part of the narrative; it is actively shaping the opportunities and risks within the capital markets.

**Exhibit 32: We Narrow the Range of Our 2025e GDP to 1.5-2.0% vs. 1.0-2.0% Previously...**

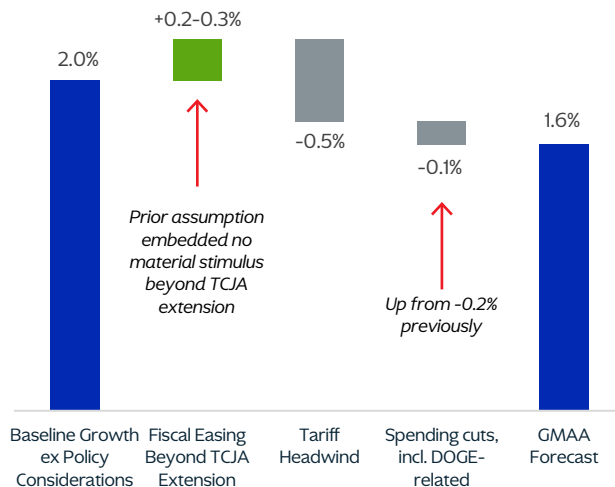
**GMAA 2025e U.S. GDP Forecast Detail**



Data as at June 15, 2025. Source: KKR Global Macro & Asset Allocation analysis.

**Exhibit 33: ...While Raising 2026e to 1.6% from 1.3%**

**GMAA 2026e U.S. GDP Forecast Detail**



Data as at June 15, 2025. Source: KKR Global Macro & Asset Allocation analysis.



**Exhibit 34: Key Productivity-Driving Sectors Include TMT, Retail, Professional Services, Leisure, and Oil and Gas**

**Productivity Growth by Industry**

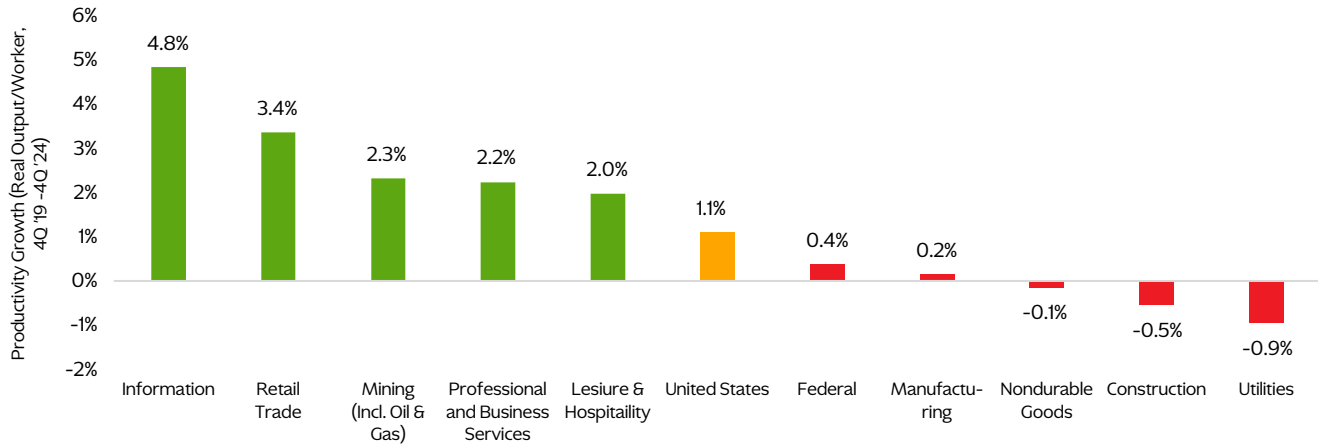
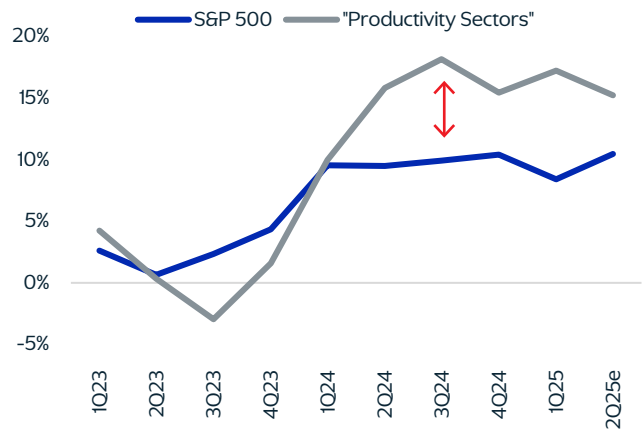


Chart considers top/bottom 5 Industries. Data as at June 10, 2025. Source: Haver Analytics, U.S. Bureau of Economic Affairs.

In a higher-cost world, productivity becomes a key differentiator, both for companies and for macro-level performance. We view it as a critical anchor for both long-term U.S. growth expectations and investing strategy. Strong productivity will be needed to allow corporate margins to hold in a world of stickier wages and lower immigration. While productivity growth is expected to moderate below 1% in 2025-2026, this deceleration is cyclical, not structural. Work done by our colleagues Brian Leung and Miguel Montoya suggests that transient pauses are normal during secular productivity expansions, and echo comparisons to the 1990s, when productivity growth fell below 1% in 25 percent of all quarters but still led to the IT productivity boom. Recall that U.S. productivity in the 1990s underwent a structural acceleration, making it one of the most important tailwinds for GDP growth, corporate profitability, and asset returns during that decade. We see signs that the longer-term productivity story remains intact, as new business formation and technology investment intentions have stayed robust despite policy uncertainty. As a result, we are focused on opportunities with enablers of productivity—workflow automation, labor market analytics, skills-based training, and job search platforms.

**Exhibit 35: Earnings in These Sectors Continue to Outperform the Broader Economy**

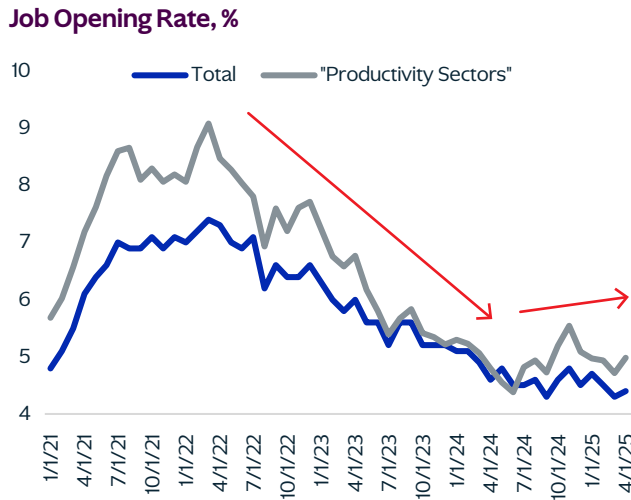
**LTM EBITDA Y/y, %**



e = Consensus bottom-up estimate per Bloomberg. 'Productivity Sectors' = Market cap weighted average of S&P 500 Info Tech, Communications Services, Commercial Services, Retail, Leisure/Hospitality, and Energy. Data as at June 15, 2025. Source: Bloomberg, KKR Global Macro & Asset Allocation analysis.

In a higher-cost world, productivity becomes a key differentiator, both for companies and for macro-level performance.

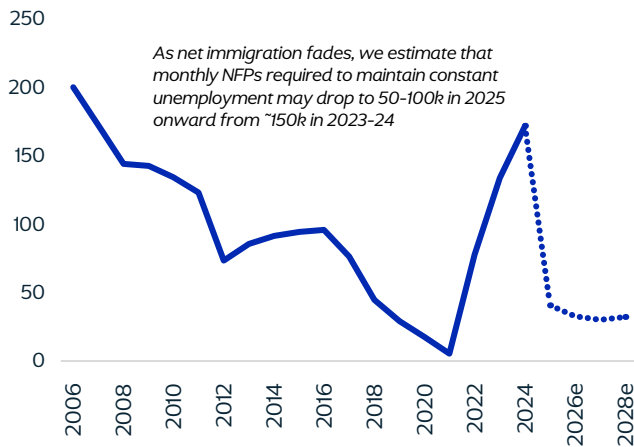
**Exhibit 36: Job Openings Have Actually Perked Up Somewhat in Productivity Sectors, Reinforcing That Fundamentals Remain Solid**



'Productivity Sectors'= Employment weighted average of Information, Professional & Business Services, Retail, Consumer Services, and Mining (Including Oil & Gas). Data as at June 15, 2025. Source: Bloomberg, KKR Global Macro & Asset Allocation analysis.

**Exhibit 37: As Net Immigration Slows, We Expect the Monthly NFPs Needed to Keep Unemployment Steady Could Fall to Around 50-100k**

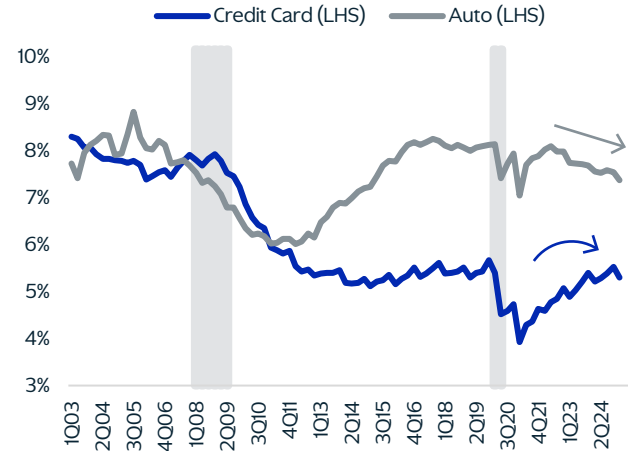
**Approximate Monthly NFP Growth Required to Maintain Constant Unemployment Rate (Thou.)**



Data as at June 10, 2025. Source: KKR GMAA estimates based on Census Bureau data and population projections.

**Exhibit 38: U.S. Consumers Are Proceeding Cautiously. Deleveraging Has Widened to Encompass Not Just Mortgage Debt, But Also Credit Card and Auto**

**Credit Card and Auto Debt as a % of Disposable Income**



Gray shading denotes recessionary quarters. Data as at June 10, 2025. Source: U.S. Bureau of Economic Analysis, Federal Reserve, Haver Analytics, KKR Global Macro & Asset Allocation analysis.

**U.S. CPI**

**Forecast:** While we already held a below-consensus CPI forecast for 2025 (2.8% vs. 3.0%), we now slightly revise this estimate downward a shade further to 2.7%. For 2026, we move to 2.9% from 3.3% but remain slightly above the consensus of 2.8%. We are experiencing a near-term soft patch in housing, which is reflected in our forecast revisions. Specifically, shelter inflation has moderated faster than expected, and we are now seeing outright pockets of softness in some sunbelt metros with short-term supply gluts.

Meanwhile, tariff-related price increases for goods are coming through more slowly than expected. Though we still expect tariffs to become more evident in the data starting in the fall, the lag we have seen thus far does serve to moderate our 2025 and 2026 forecasts slightly.

We also continue to remain below-consensus on energy prices and have reflected that view more concretely in our CPI outlook for 2H25-2026, particularly as risks of broad Iran-related supply disruptions in the Gulf have moderated.

Longer term, though, we still ascribe to our higher resting heart rate for inflation thesis. Indeed, while tariffs are not generating immediate and outsized CPI pressure just yet (as evidenced by our forecast of CPI in the 2.7% to 2.9% range for the next 18 months), we think that they will prevent inflation from falling faster than it normally would. Key milestones on future inflation trends include the rollout of 2026-model consumer goods as well as the back-to-school retail cycle in the fall.

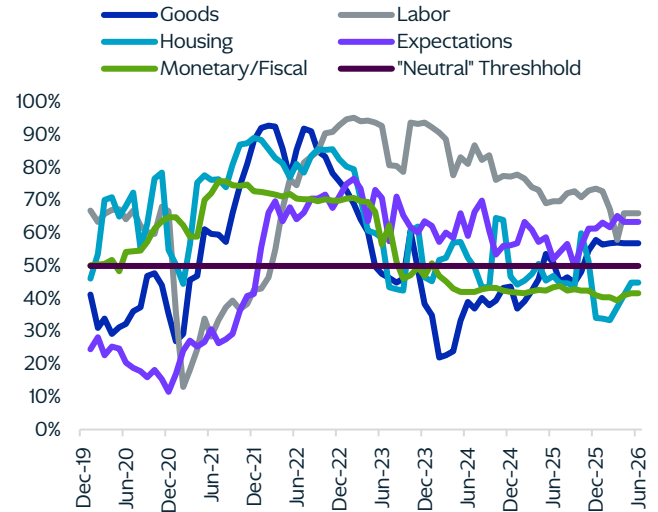
**Commentary:** Our base case continues to call for core inflation to remain sticky, hovering around 3% over the next two years. Key to our thinking is that we still expect higher goods inflation from tariffs, particularly as 2026-year models are released for autos and electronics. Meanwhile, we think higher goods costs post-tariffs could also put more pressure on consumer inflation expectations, which will show up in more modest than normal services disinflation at this point in the cycle. In particular, shelter inflation looks poised to become less disinflationary heading into 2026, as lower construction starts and higher insurance costs feed through the system, we believe.

From a policy perspective, tariffs represent a structural supply shock that will likely embed a floor under goods prices. In our high-case scenario, where tariffs escalate beyond our base assumptions, inflation could push higher, though we see that path as less probable given recent stabilization in trade ‘rhetoric’. At the same time, our base case forecasts assume that energy prices remain subdued amid weaker fundamentals. If geopolitical risks around Iran and Russia returned to the fore and pushed oil prices higher, and/or if OPEC+ market management were more disciplined than what we envision, we would see further upside risks to consumer expectations and realized inflation.

For investors, the implication is clear: while inflation is not running away, it is also not reverting to pre-pandemic norms. As such, we suggest that all allocators of capital position their portfolios accordingly, including beefing up exposure to Real Assets, including inflation-linked cash flows as well as collateral-based assets tied to nominal GDP. Meanwhile, we also believe tariff uncertainty and the impact on inflation continues to accentuate preexisting trends towards 1) a steeper curve and 2) a weaker USD.

**Exhibit 39:** Aside from an Ongoing Reacceleration in Goods Inflation, We Are Most Focused on the Potential for Owner’s Equivalent Rent to Increase

**Leading Inflation Dashboard Components (Indicator Levels as a Percentile of Range Since 2001 With Relevant Leads Applied)**

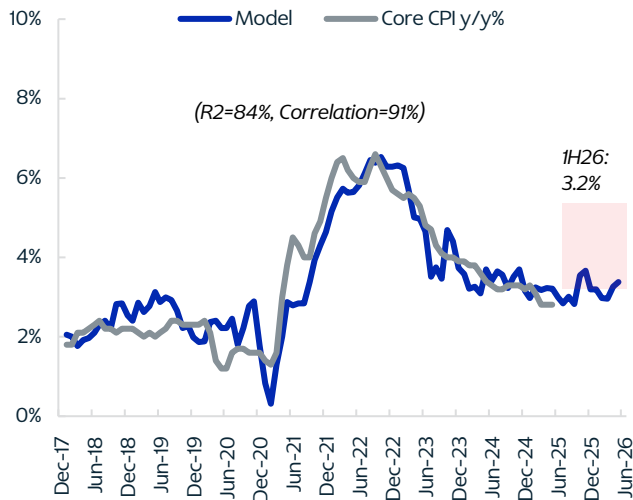


Model inputs as % of historical range, with relevant leads applied. Data as at June 30, 2025. Source: Bloomberg, U.S. Bureau of Economic Analysis, Haver Analytics, KKR Global Macro & Asset Allocation analysis.

Longer term, though, we still ascribe to our higher resting heart rate for inflation thesis. Indeed, while tariffs are not generating immediate and outsized CPI pressure just yet, we think that they will prevent inflation from falling faster than it normally would.

**Exhibit 40:** Our Model Points to Run-Rate Inflation in the Low-Mid Three Percent Range in 1H26, a View That Includes Firmer Rental Inflation

**Core CPI Leading Indicator**



Model refit monthly to ensure that forward-looking projections reflect most relevant inflation drivers. Data as at June 6, 2025. Source: Bloomberg, U.S. Bureau of Economic Analysis, Haver Analytics, KKR Global Macro & Asset Allocation analysis.

**Euro Area GDP**

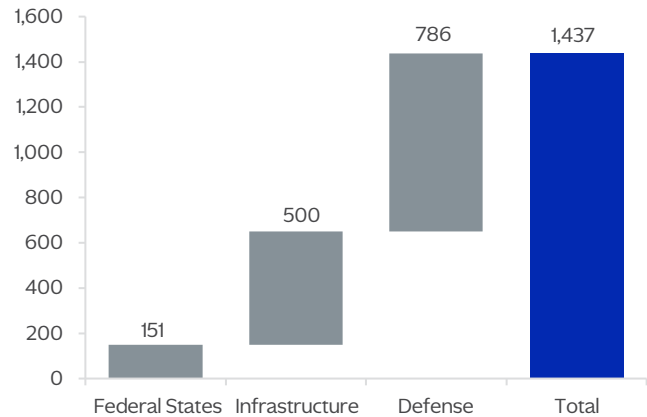
**Forecast:** We have revised our Eurozone Real GDP growth forecast upward to 0.9% in 2025 (from 0.7% and in line with consensus at 0.9%) and maintain our above-consensus call of 1.3% in 2026 vs. consensus of 1.1%, supported by a combination of fiscal expansion, easing monetary policy, and structurally tight labor markets. We are now incrementally more constructive on Eurozone growth through 2026, driven by a meaningful shift in fiscal policy, a more stimulative real rate environment, and continuing improvement in macro fundamentals in the European periphery.

**Commentary:** A key driver of our more optimistic outlook is Germany’s recently announced €1.4 trillion fiscal package, heavily focused on boosting defense and infrastructure investment. The scale and composition of this stimulus are expected to provide a meaningful boost to aggregate demand and stimulate investment activity, with tangible growth effects beginning to surface in late 2026. While trade tensions remain a downside risk, there are other positives to note: labor markets across the Eurozone continue to hold up well and European equities

are showing signs of renewed strength, closing the performance gap with the U.S.

**Exhibit 41:** Germany Plans On Spending an Additional Third of Its Current GDP Over the Next 12 Years, Underpinning the Optimism for Europe

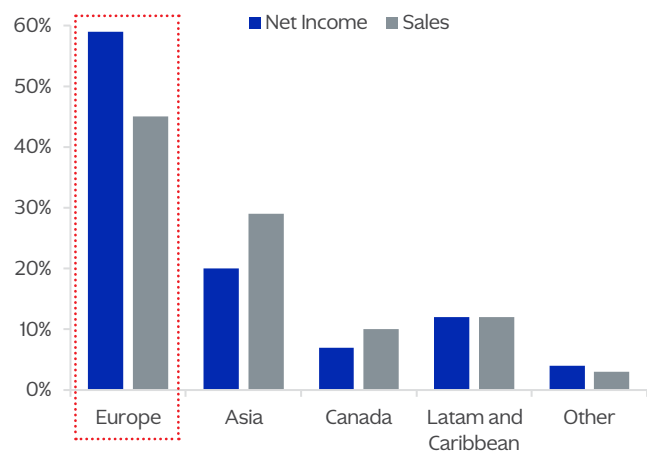
**Germany Proposed Fiscal Packages: Potential Volume Over Next 12 Years, EUR Billions**



Data as at March 6, 2025. Source: Deutsche Bank, Federal Statistics Office.

**Exhibit 42:** Europe Is the Most Important International Market for U.S. Corporates. Not Only Is It About 60% of International Profit, But Europe Is Also Significantly Margin Accretive

**U.S. Multinational Enterprises: Share of Profit and Top Line by Majority Owned Affiliates (2022)**



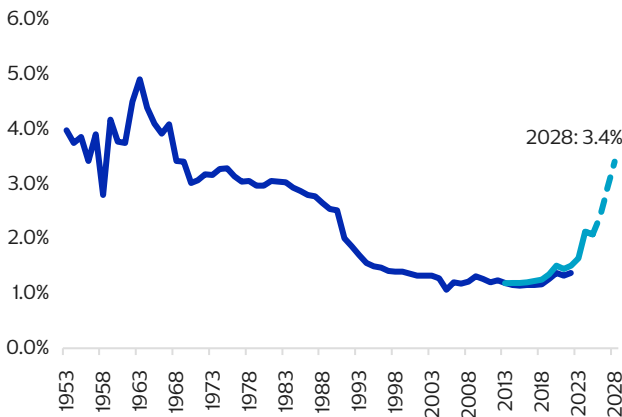
Data as at December 31, 2022. Source: BEA, Deutsche Bank.

However, trade tensions with the U.S. are unlikely to resolve quickly and remain a key risk this year. The gap between the EU and the U.S. will be more challenging to bridge than that with the U.K., with effective tariff rates likely stabilizing around 20%. Meanwhile, the EU is considering retaliatory tariffs on approximately €95 billion worth of U.S. goods, targeting sectors like aerospace, autos, and medical equipment during ongoing negotiations.

Looking beyond this year, Germany’s fiscal pivot could be a game-changer for Europe’s medium-term growth. Committing to an additional €1.4 trillion in public spending—about a third of Germany’s GDP—over the next decade across defense, infrastructure, and public services introduces significant upside potential for European growth.

**Exhibit 43:** German Defense Spending Could Exceed 3% of GDP As Early As 2027, a Level Not Seen Since Before Reunification

**Germany Defense Spending as a % of GDP**

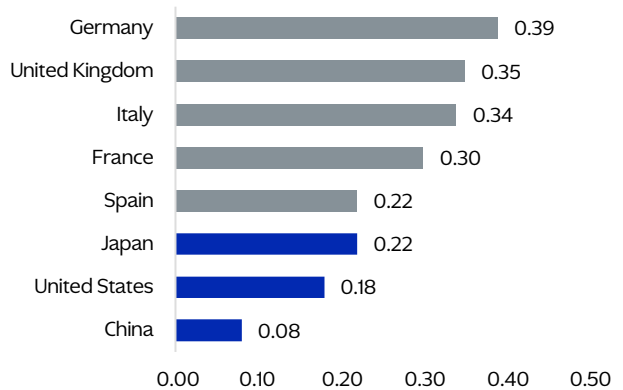


Data as at June 5, 2025. Source: SIPRI, NATO, UBS.

Looking beyond this year, Germany’s fiscal pivot could be a game-changer for Europe’s medium-term growth.

**Exhibit 44:** In 2024, Household Electricity Prices Were Still Double U.S. Levels Across Most of Europe

**Global Household Electricity Prices, 2024, USD/KWH**



Data as at December 31, 2024. Source: Global Petrol Prices.

Energy prices across Europe remain elevated relative to global peers, continuing to weigh on consumers and manufacturers. In 2024, household electricity prices in most European countries were more than double those of the U.S., with Germany, the U.K., and Italy among the most expensive. The path to energy resilience hinges on accelerating grid upgrades, stabilizing input costs, and balancing energy security with decarbonization efforts—critical steps to restoring industrial competitiveness and ensuring a reliable, low-carbon energy supply in Europe.

What does this mean for investing? We think the focus should be on key themes, including:

**Security of Everything:** Persistent geopolitical tensions reinforce our ‘Security of Everything’ thesis, and we believe these tensions will accelerate Europe’s push towards greater strategic autonomy. To capitalize on this shift, we think investors should allocate to assets and platforms that foster resilience: grid infrastructure, reshoring initiatives, cybersecurity, and localized manufacturing. Europe’s policy environment is increasingly aligned with these priorities, and private capital will be essential in transforming strategic intent into real-world execution.

**Periphery-Led Growth:** A decade of deleveraging, EU fund deployment, and competitiveness improvements has made southern Europe structurally stronger and more attractive than in the past. While economic momentum in the periphery continues to outpace the core, credit



remains shallow as many of these markets are still underbanked. This creates a compelling opportunity, in our view, to target credit strategies aligned with the recovery and the catch-up in capital deployment across the region.

**Public-to-Privates:** Europe has narrowed much of its performance gap with the U.S., yet it still trades at a meaningful discount. The recent rally has been led by domestic names—industrials, financials, and utilities. We think the real public-to-private opportunity lies in local leaders with strong earnings but compressed multiples.

**Labor Market Tightness:** Despite some softening indicators, labor markets across Europe remain tight as companies hoard talent. To manage wage-driven margin pressures, focus on automation, digitization, and strategic offshoring.

**Capital Markets Union and Securitization:** Europe will need an estimated €1 trillion annually in new investments to boost productivity. Policymakers are working to unlock growth through a more developed savings and investment union and a tailored securitization framework, with the potential to direct some of the €33 trillion of EU household savings to more productive uses. We believe this structural shift will be key to unlocking Europe’s long-term growth potential.

## Euro Area CPI

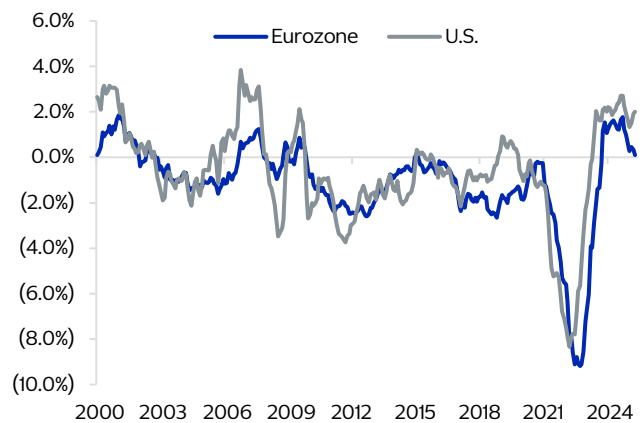
**Forecast:** We forecast Eurozone inflation to average 1.9% in 2025 and 2.0% in 2026, modestly below our prior estimates of 2.1% for both years and broadly in line with the ECB’s target, reflecting faster-than-expected goods disinflation and a more balanced energy outlook. These projections remain slightly above consensus, which stands at 2.0% and 1.9% for 2025 and 2026, respectively, due to continued wage pressures, fiscal stimulus, and stickier service-sector inflation.

**Commentary:** While disinflation has progressed across goods and energy, we remain mindful of stickier components, notably shelter, services, and labor-driven input costs. Structurally tight labor markets continue to anchor wage growth, and fiscal stimulus, especially Germany’s €1.4 trillion 10-year spending package, adds upside risk to both demand and price pressures. That said, real rates are now clearly stimulative, and with inflation

expectations stable, the ECB retains policy flexibility. We anticipate one final rate cut this year, with easing already filtering into credit and lending conditions. Looking ahead, energy price volatility, tariff impacts, and labor hoarding dynamics will be key inflation watchpoints as we assess the durability of the disinflation trend.

### Exhibit 45: Real Rates in Europe Are Much More Stimulatory Than in the U.S., With Close to 0% Real Rates Providing a Tailwind to the Economy

**Real Rates (Bank Rate Minus CPI inflation): U.S. vs. Europe**



Data as at April 30, 2025. Source: ECB.

## China GDP

**Forecast:** We have raised our 2025 China GDP forecast to 4.7% (vs. 4.5% consensus) due to earlier-than-expected tariff relief. However, growth is likely to slow in H2 as export frontloading fades and 30% tariffs take effect. Our 2026 forecast remains at 4.1%, in line with consensus.

**Commentary:** Our previous forecast assumed harsher tariffs, so partial relief prompted an upward revision. Still, China’s growth is expected to slow from 5.4% y/y in 1Q25 to 4.0% by 1Q26, reflecting external pressures, housing correction, labor softness, and a shift towards domestic demand. Tackling nearly three years of deflation remains key. Thus, we expect further fiscal stimulus beyond the current 8.4% of GDP deficit and additional monetary easing in H2.

**Point #1:** The earlier-than-expected partial tariff relief helped offset some of the damage from reciprocal tariffs, reducing the estimated growth impact from -240 basis points (under a 145% tariff) to 'just' -90 basis points (under a 30% tariff). However, the 30% tariff remains substantial and could threaten up to 3.8 million manufacturing jobs. Sectors facing a combined 55% tariff (25% existing + 30% additional), such as home appliances, are under pressure as the elevated costs may erase Chinese brands' typical 30-50% price advantage over Japanese and German competitors. As a result, growth momentum is expected to slow notably over the next 3-4 quarters.

**Point #2:** The housing market correction is still a significant headwind for 2025, though we now believe it is more than halfway completed. Our correction index, which tracks sales, prices, and starts, has dropped over 30%, aligning with post-bubble patterns in Japan, the U.S., and Spain. Real Estate's share of GDP has fallen by over 10ppt to 15% in the past three years, suggesting a milder correction ahead (likely another 5ppt over five years). Still, the drag on 2025 growth is expected to be around -1.5ppt. Overall, housing activity remains weak amid the fading stimulus effect and tariff-related uncertainty.

**Point #3:** China's consumer sector remains under pressure, weighed down by a weak job market and slow recovery in high-paying industries like IT, finance, and semiconductors. The potential loss of 3.8 million factory jobs further dampens confidence, keeping spending well below pre-COVID levels. With low consumption propensity and rising excess savings, a quick rebound remains unlikely.

**Point #4:** Having highlighted these key challenges to China's economy, we do see resilience and positive trends emerging in the economy:

- **Technological Innovation:** Breakthroughs in AI, robotics, space, and biotech are accelerating. China's pharmaceutical sector, for instance, saw a surge in licensing revenues, with large pharma in-licensing 28% of innovator drugs in 2024. Total deal value involving Chinese biopharma licensors rose 66% y/y to \$41.5 billion in 2024, a five-year high.<sup>1</sup>

- **Consumer Brand Momentum:** Gen-Z-led brands offering emotional and lifestyle value are outperforming traditional players. Sectors like art toys, trendy food & beverage, pet care, cosmetics, and medical aesthetics are gaining traction.
- **Policy Support:** The government is intensifying efforts to combat deflation, raising the budget deficit from 6.6% to 8.4% in 2025. It's also addressing overcapacity through tighter standards, industry consolidation, and stronger guidance for emerging sectors like semiconductors, EVs, and biopharma.
- **Asset Market Stabilization:** The gradual recovery in equity markets, alongside some stabilization in the housing market are helping to repair household balance sheets.

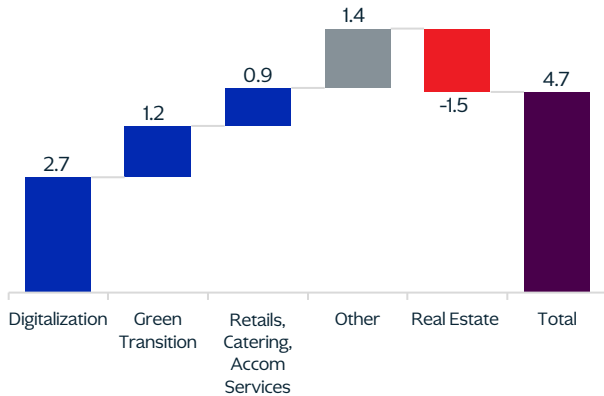
**Bottom Line:** We have revised up our 2025 growth forecast following earlier-than-expected tariff relief, though momentum is likely to slow as the impact of the 30% tariff unfolds. China's growth is expected to moderate from 5% to a more sustainable 4% over the next few quarters, with deflation control remaining a key policy focus. Nonetheless, early signs of long-term resilience are beginning to emerge.

The housing market correction is still a significant headwind for 2025 in China, though we now believe it is more than halfway completed.

<sup>1</sup> GlobalData's Pharma Intelligence Center Deals Database.

**Exhibit 46:** By Sector, Real Estate Remains the Main Drag on Growth

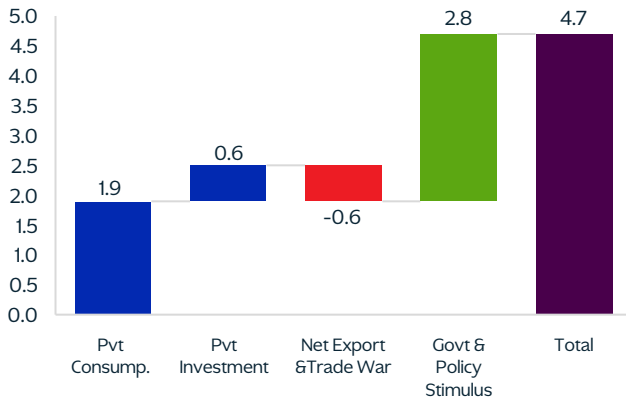
**China GDP Breakdown by Sector (2025)**



'Green transition' is based on green finance and transition investment studies from the Beijing Institute of Finance and Sustainability as well as reported by BNEF. 'Digital economy' added value is as reported by CAICT, including added value of the information industry (core digital) and added value that the information industry brings to other industries (core part: roughly 10% of the economy; overall: ~45%). Real Estate's drag is estimated by the KKR GMAA team with an IO table and includes the Real Estate industry itself and the industry's impact on upstream and downstream. 'Other' represents the other half of the economy, i.e., agricultural, industrial, and services other than digital, green industries, catering and accommodation and retail services. Data as at July 10, 2025. Source: Beijing Institute of Finance and Sustainability, China National Bureau of Statistics, BNEF, CAICT, KKR Global Macro & Asset Allocation analysis.

**Exhibit 47:** Digitalization and Green Transition Propel China's Growth Amid Housing Sector Struggles

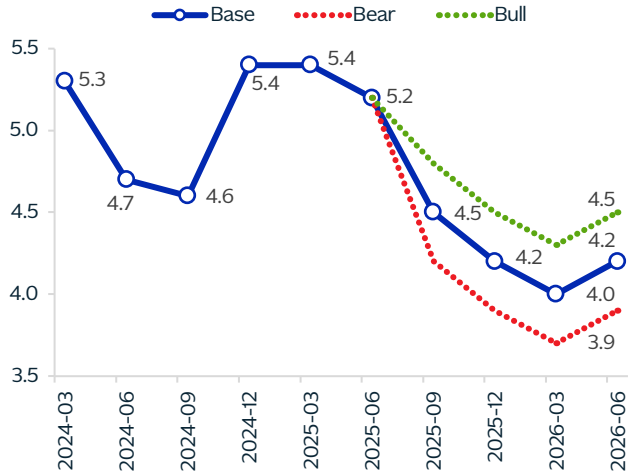
**China GDP Expenditure Sector Breakdown (2025)**



Data as at June 23, 2025. Source: China National Bureau of Statistics, Haver Analytics, KKR Global Macro & Asset Allocation analysis.

**Exhibit 48:** China's Quarterly Growth Momentum May Unavoidably Slow As Frontloaded Trade Effects Dissipate and Higher Tariffs Are Phased-in

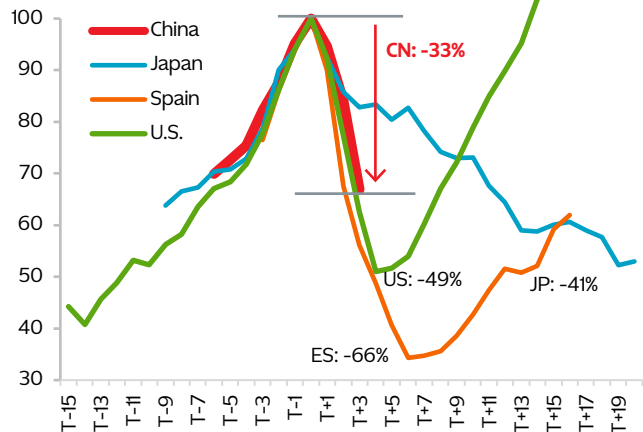
**China GDP Growth Outlook, % Y/y**



We assign a 55% probability to our base case, 30% to the bear case, and 15% to the bull case. Data as at June 30, 2025. Source: China National Bureau of Statistics, Haver Analytics, KKR Global Macro & Asset Allocation analysis.

**Exhibit 49:** The China Housing Market Correction Index Is Down 33% From Peak, Suggesting We're Over Halfway Through the Correction

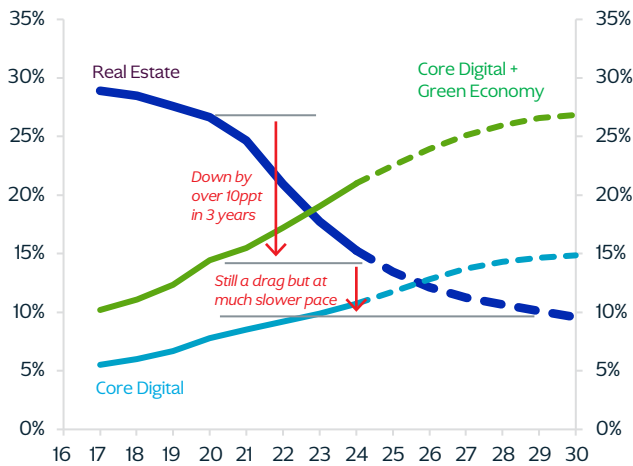
**Housing Market Correction Index: China vs. U.S., Japan and Spain**



Housing Market Correction Index is the simple average of correction index for housing price, investment and starts. Year T is the peak of housing bubble, which is 2021 for China. Data as at December 31, 2024. Source: Japan Ministry of Land, Infrastructure and Transport, China National Bureau of Statistics, Federal Housing Finance Agency, Census Bureau, Spanish Statistical Office, Haver Analytics, KKR Global Macro & Asset Allocation analysis.

**Exhibit 50:** Real Estate's Share of GDP Growth May Stabilize After a 10-15ppt Drop Over 3-4 Years, While Digital and Energy Sectors Power a Structural Economic Shift

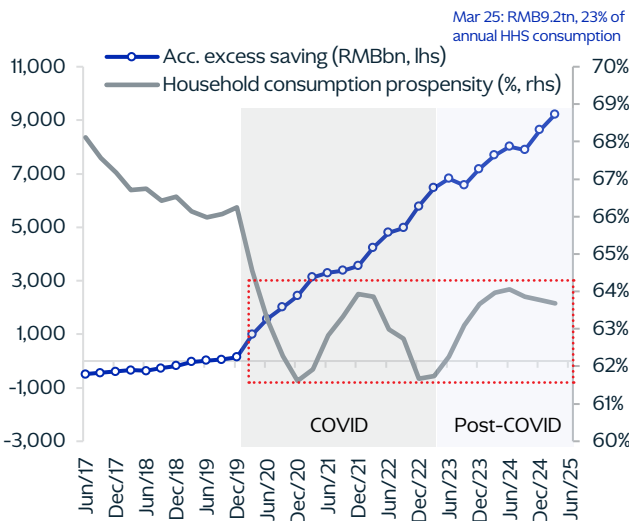
**Share of China GDP**



Core digital industries refer to industries that rely entirely on digital technologies, as well as provide technologies for the digitalization of other industries. Green economy includes clean energy, electrified transport, clean industry, etc. Data as at December 31, 2024. Source: CNBS, BNEF, CAICT, KKR Global Macro & Asset Allocation analysis.

**Exhibit 51:** Consumer Confidence Has Tumbled in China, Which is Leading to Weak Consumption and High Savings Rates

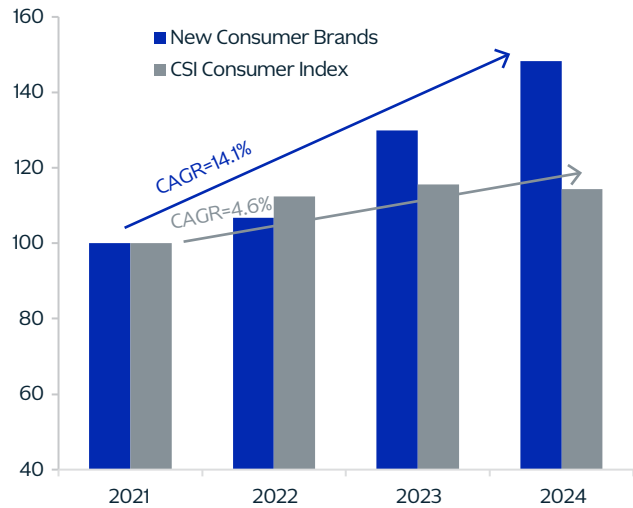
**China: Accumulated Excess Saving vs. Consumption Propensity**



Acc. excess saving is calculated as accumulated saving above the pre-COVID saving ratio baseline level, from 2020 onward. Data as at May 30, 2025. Source: China Customs, Wind, KKR Global Macro & Asset Allocation analysis.

**Exhibit 52:** However, Gen Z and the 'New Consumerism' Are Blossoming. Indeed, Emerging Brands in Art Toys, Trendy F&B, Pets, and Beauty Are Growing at 14.1% CAGR, Triple Traditional Sector Growth in Recent Years

**Total Revenue of Consumer Companies (2021=100)**



New consumer brands include 39 listed companies in sectors favored by Gen Z, such as art toys, trendy food and beverages, pet care, cosmetics, jewelry, and medical aesthetics. In comparison, the CSI Consumer Index comprises 40 listed companies across more traditional sectors, including dairy, alcoholic beverages, condiments, pig farming, jewelry, and pet-related businesses. Data as at December 31, 2024. Source: Bloomberg, Wind, KKR Global Macro & Asset Allocation analysis.

**China Inflation**

**Forecasts:** We have lowered our 2025 CPI forecast from 0.5% to 0.3%, aligning with market consensus. For 2026, we expect inflation to reach 0.7%, below the consensus estimate of 1.0%.

**Commentary:** Deflation remains a key challenge and policy priority amid persistent overcapacity and weak demand. As of May, the PPI has been negative for 32 consecutive months, and CPI has also dipped into negative territory. The domestic supply-demand imbalance is driving sustained deflationary pressure, which the trade war is likely to intensify. Drawing on Japan's experience, addressing deflation requires both market clearing and aggressive monetary easing. This implies unavoidable deleveraging and consolidation in the property and related sectors, alongside efforts to lower real interest rates.

## Japan GDP

**Forecasts:** We have cut Japan's 2025 growth forecast to 0.7% (vs. 0.8% consensus) on external risks while keeping our 2026 forecast at 0.8%, slightly above consensus (0.7%).

**Commentary:** Japan's growth faces external risks from U.S. auto tariffs and cost-push inflation driven by rising rice and oil prices. These pressures may ease in the second half of 2025 potentially with a trade deal and reduced geopolitical tensions. Domestically, structural reforms, corporate reshoring, and tech-focused investment are boosting profits and productivity. Wage growth, supported by a tight labor market, is strengthening consumer demand. For allocators, this reinforces the case for increased Japan exposure, especially in real asset-heavy sectors, innovation-linked capex plays, and domestic-focused consumer growth.

**Point #1:** Tariff hikes and global uncertainty may cut Japan's GDP by 40 basis points. The U.S., which is its top trading partner, accounts for 20% of exports, including 40% of autos and 25% of auto parts. With 10% tariffs on goods and 25% on autos, export prices fell in May (total: -3.5%, autos to U.S.: -9.8%). Automakers are absorbing costs to protect market share while awaiting a trade deal.

**Point #2:** Despite recent cost-push inflation, Japan's domestic demand remains on track, supported by strong wage growth driven by labor shortages and solid demand. The 2025 Shunto negotiations delivered a 3.8% base pay hike—the highest since 1990—underpinned by robust corporate earnings. With wages still 20% below Korea's and less than half of U.S. levels, there is room for sustained growth. As inflationary pressures, mainly from food and energy, are expected to ease in 4Q25, we remain confident in the continued recovery of real incomes and household spending.

**Point #3:** Corporate reforms and strong profitability are driving Japan's Capex rebound. Governance changes—more independent directors, shareholder empowerment, performance-based pay, and reduced cross-shareholding—have boosted efficiency and returns. Since 2023, corporate profits have grown at an 11% CAGR, far outpacing the approximate 4% nominal GDP growth. Investment is rising, especially in software,

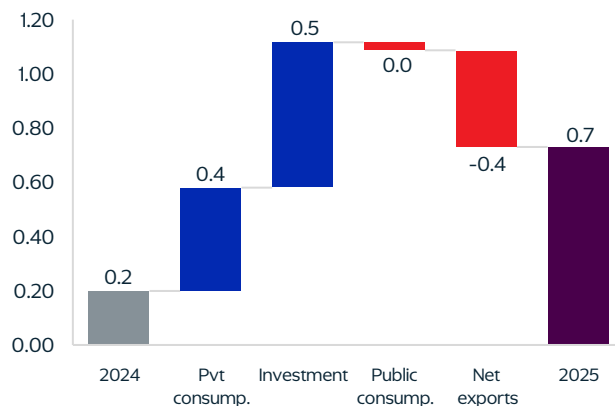
with pent-up demand for equipment renewal, capacity expansion, and infrastructure upgrades supporting continued growth.

**Point #4:** With the July 2025 Upper House election nearing, the ruling Liberal Democratic Party (LDP) risks losing its Upper House majority, which could shift internal power dynamics and stall broader reform momentum. Fiscal policy is under scrutiny as opposition parties propose consumption tax cuts, including targeted food exemptions as well as a broad reduction in the consumption tax rate, potentially costing up to 2.3% of GDP annually. Combined with rising defense spending pressures from the U.S., such measures could strain fiscal space, undermine debt sustainability, and destabilize the JGB market, potentially pushing yields higher than expected.

**Bottom Line:** Japan is navigating a weak external environment but showing solid domestic momentum. Wage growth, corporate reform, and expanding capex support a positive recovery outlook, despite headwinds from goods inflation and tariff uncertainty. We continue to see strong investment potential in areas such as corporate restructuring, digital transformation, automation, health and wellness (e.g., fighting loneliness), and rising demand for asset management.

**Exhibit 53:** U.S. Tariff Hikes May Trim Japan's GDP by 40 Basis Points...

**Japan GDP Growth Breakdown (ppt)**

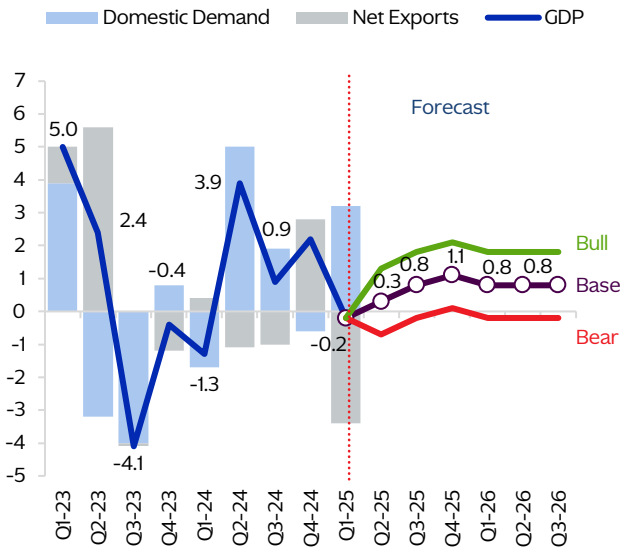


Data as at June 23, 2025. Source: Cabinet Office of Japan, Haver Analytics, KKR Global Macro & Asset Allocation analysis.



**Exhibit 54:** ...That Said, Sequential Growth Is Still Expected to Pick Up in 2H25

**Japan: Quarterly Real GDP (SAAR, %)**



We assign a 60% probability to our base case, 20% to the bear case, and 20% to the bull case. Data as at March 31, 2025. Source: Cabinet Office of Japan, Analytics, KKR Global Macro & Asset Allocation analysis.

Since 2023, corporate profits in Japan have grown at an 11% CAGR, far outpacing the approximate 4% nominal GDP growth. Investment is rising, especially in software, with pent-up demand for equipment renewal, capacity expansion, and infrastructure upgrades supporting continued growth.

## Japan Inflation

**Forecast:** Stronger-than-expected rice and oil prices have lifted our 2025 CPI forecast to 2.7% (up from 2.0%), just shy of the 2.8% market consensus. For 2026, we anticipate inflation to moderate to 1.8%, aligning with consensus expectations.

**Commentary:** The May CPI headline at 3.5% y/y and core-core at 3.3% reflects robust short-term inflation momentum. Near-term inflation will largely depend on the success of government efforts to lower rice prices. Although early signs of price declines point to a potential 4Q25 slowdown, broadening food inflation and geopolitical tensions may moderate the pace of deceleration. Core CPI is expected to remain above 2% through year-end. Looking ahead, a healthier wage-inflation spiral and recovering consumption should help sustain inflation at around 2%.

## SECTION III

# Capital Markets

## S&P 500

**Forecasts:** Our colleague Brian Leung now expects the S&P 500 to reach 6,550 in 2025 and 7,110 in 2026 under our base case (50% probability), which implies roughly 14% upside from current levels over the next 18 months. On the earnings front, he forecasts 8% year-over-year EPS growth in 2025 (to \$264 per share), slightly above the 'top-down' consensus estimate of \$259 per share. For 2026, he expects EPS to reach \$291 per share (10% year-over-year growth), which is broadly in line with consensus. On valuations, he assumes equity multiples can expand

modestly to 22.5-23.0x forward earnings from 22.0x today. This outlook is anchored in our view that the current market cycle still has room to run and that financial conditions could remain favorable as the Fed lowers interest rates and concludes its quantitative tightening program. While we expect tariffs to weigh on earnings growth, we do not believe that they will be sufficient to derail the cycle. We also expect that more clarity around the new Fed governor, tariffs, and capex spending in 2026 relative to 2025 will help support risk assets again over the next 18 months.

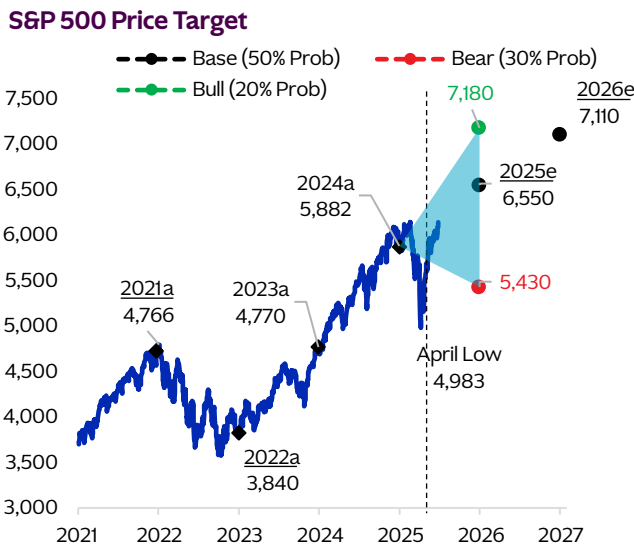
**Exhibit 55:** Given All the Volatility, We Have Been Using More Scenario Analysis to Underwrite Our Outlook

### S&P 500 Price Target Scenarios

Current = 6,227	Base (50% Prob)	Bear (30% Prob)	Bull (20% Prob)	Weighted Average	Bottom-Up Consensus	Top-Down Consensus
2025 Year-End Target	6,550	5,430	7,180	6,340	n/a	5,939
P/E on 2026 EPS	22.5x	21.8x	22.9x	22.4x		
2026 Year-End Target	7,110	n/a	n/a	n/a	n/a	n/a
P/E on 2027 EPS	22.9x	n/a	n/a			
2023a EPS	\$224	\$224	\$224	\$224	\$224	\$224
2024a EPS	\$245	\$245	\$245	\$245	\$245	\$245
2025e EPS	\$264	\$228	\$275	\$256	\$263	\$259
2026e EPS	\$291	\$249	\$314	\$283	\$300	\$287
2027e EPS	\$311	\$259	\$339	\$301	n/a	n/a

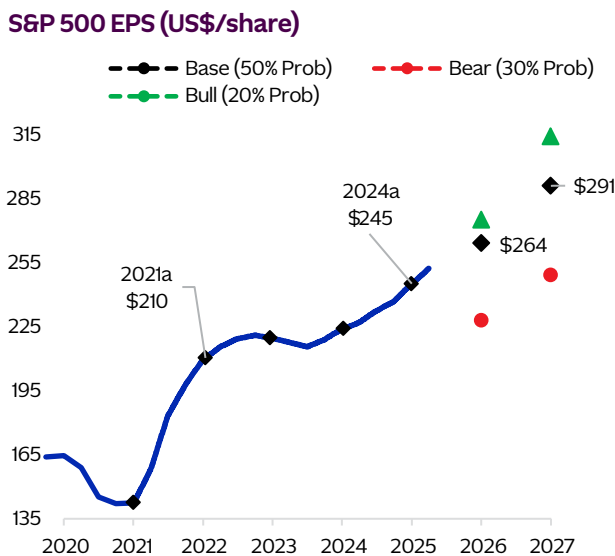
Data as at July 2, 2025. Source: Bloomberg, Haver Analytics, KKR Global Macro & Asset Allocation analysis.

**Exhibit 56:** We Expect the S&P 500 to Reach Around 6,550 in 2025 and 7,110 in 2026



Data as at July 2, 2025. Source: Bloomberg, Haver Analytics, KKR Global Macro & Asset Allocation analysis.

**Exhibit 57:** Our Base Case Has S&P 500 EPS Reaching \$264 Per Share in 2025 and \$291 per Share in 2026



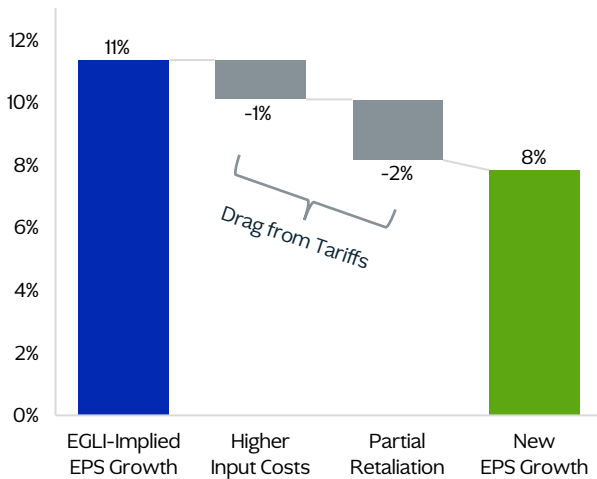
Data as at July 2, 2025. Source: Bloomberg, Haver Analytics, KKR Global Macro & Asset Allocation analysis.

**Commentary:**

- On EPS:** We project S&P 500 EPS to grow by 8% in 2025, reaching \$264 per share. This is slightly above the current ‘top-down’ consensus estimate of \$259 per share, but lower than our start-of-year forecast of \$273 per share. Our base case assumes a weighted average tariff rate of roughly 17%, which we estimate will result in a 3% drag on EPS. Our forecasts reflect both higher input costs (which are partially absorbed through margins) and anticipated foreign retaliation (hurting international sales). Notably, we are encouraged by how the ‘Magnificent-7’ stocks continue to exhibit strong fundamental performance, posting 28% year-over-year EPS growth in 1Q25 (an 11% earnings surprise) and providing strong guidance on AI-related capital expenditures. Looking ahead, we see S&P 500 EPS growth possibly accelerating to about 10% in 2026, supported by global interest rate cuts, a weaker U.S. dollar, benign oil prices, and a more business-friendly policy environment (including deregulation and tax incentives such as bonus depreciation). As shown in *Exhibit 14*, the U.S. dollar leads earnings growth by about 12 months (so USD weakness should not materially impact 2025 earnings) and will provide an approximate 60 basis points boost to 2026 EPS.
- On Valuations:** Our outlook for 2025-26 assumes equity market multiples can expand modestly to 22.5-23.0x NTM P/E from 22.0x today. While headline S&P 500 valuations look high compared to historical norms, they actually appear more reasonable when accounting for the index’s shift towards ‘asset-lite’ sectors and structurally higher-quality companies (with better ROIC and structurally higher profit margins following the 2017/18 corporate tax cut). On a sector- and quality-adjusted basis, valuations are elevated but not excessive, in our view. One can see this in *Exhibit 59*. Additionally, equity positioning among systematic strategies (e.g., volatility control, risk parity, and CTAs) remains modest despite the recent rally, which should provide a steady bid for equities as these strategies re-leverage.

**Exhibit 58:** Our Base Case Incorporates an Approximate 3% Tariff Hit to 2025 EPS, Reflecting Higher Input Costs (Eating Into Margins) and Anticipated Retaliation (Hurting Foreign Sales)

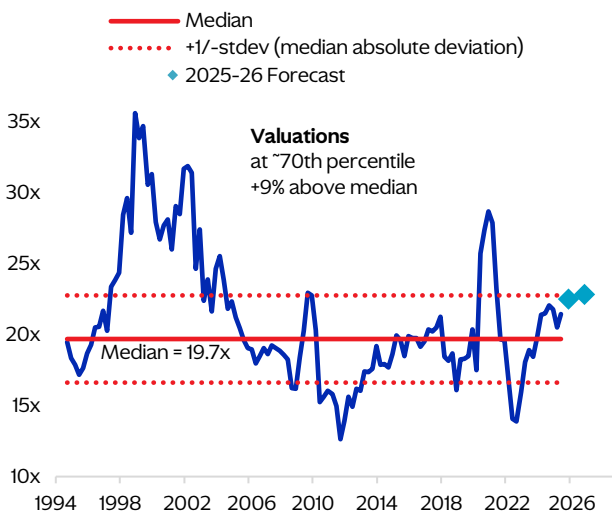
**SGP 500 EPS Growth Base Case Forecast (2025)**



'Partial retaliation' assumes partial retaliation by China, Europe, and Canada, but minimal retaliation by Mexico and RoW. Data as at July 2, 2025. Source: S&P, Bloomberg, Haver Analytics, KKR Global Macro & Asset Allocation analysis.

**Exhibit 59:** On a Sector- and Quality-Adjusted Basis, S&P 500 Valuations Are Elevated but Not Excessive, in Our View

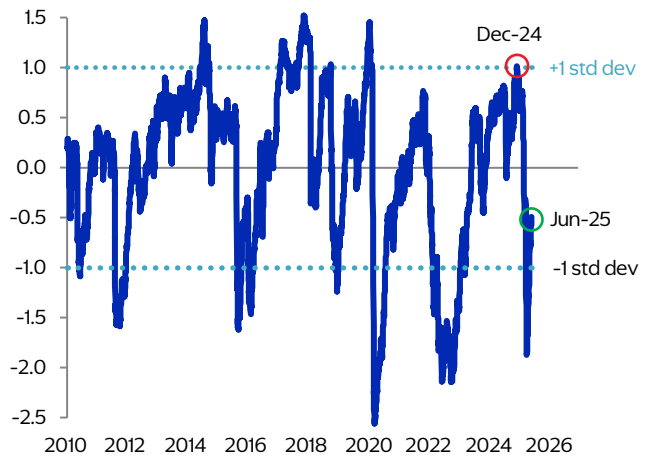
**SGP 500 Sector & Quality-Adj NTM P/E**



Quality refers to ROIC, net profit margins and operating margins. For each sector, we adjust the historical earnings by the delta in ROIC and margins back then versus today. Data as at July 2, 2025. Source: S&P, Bloomberg, Haver Analytics, KKR Global Macro & Asset Allocation analysis.

**Exhibit 60:** Systematic Strategies (Vol Control, CTAs, and Risk Parity Funds) Still Have Significant Capacity to Increase Their Equity Exposure. As These Strategies Re-Leverage, They Could Provide a Steady Source of Demand for Equities

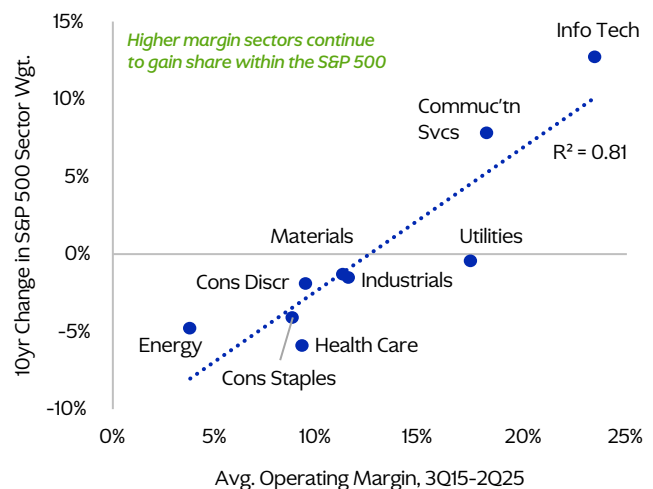
**Consolidated U.S. Equity Positioning (Weighted Avg. Z-Score of Systematic Indicators)**



Systematic strategies: CTA portfolio weight, Risk-Parity portfolio weight, Vol control allocation, equity futures positions. Data as at July 2, 2025. Source: S&P, Bloomberg, DB Research.

**Exhibit 61:** The S&P 500 Is Now a Higher Quality Index and Asset-Lite Sectors Such as Technology and Communications Continue to Gain Market Share

**SGP 500: Sector Weights vs. Operating Margin**



Data as at July 2, 2025. Source: S&P, Bloomberg, Haver Analytics, KKR Global Macro & Asset Allocation analysis.

- **Bear Case (30% probability):** Technology earnings disappoint, the housing market remains stagnant due to high mortgage rates, and a slowing labor market leads to higher layoffs. Stagflationary policies—such as reduced immigration, widespread tariffs, and ongoing Fed meddling—dominate, with little support from deregulation or new fiscal impulse. Rising concerns about fiscal sustainability push up inflation expectations and the term premium. Earnings decline about 7% year-over-year, weighed down by tariffs, and the S&P 500 finishes the year at approximately 5,400.
- **Bull Case (20% probability):** Following a soft patch in the first half of 2025, labor productivity resumes its strong post-COVID uptrend, resulting in above-trend GDP growth, disinflation, and benign financial conditions. The administration continues to roll back tariffs and emphasizes pro-growth policies such as deregulation, reshoring, and tax cuts. Both technology and cyclical stocks drive the S&P 500 to new highs of approximately 7,200 by year-end 2025.

**Our Bottom Line: We believe the current cycle still has room to run. However, given heightened policy uncertainty, we expect earnings growth—not multiple expansion—to be the primary driver of further S&P 500 gains.** Within the U.S., we favor high-quality, large-cap companies with strong pricing power, profitability, and scale. Looking internationally, we see potential for stocks in Europe and the Emerging Markets to become more competitive with U.S. Equities, especially if the U.S. dollar remains weak. This outlook is based on several factors: a) fiscal policy convergence (rest-of-world turning more expansionary just as U.S. fiscal stimulus moderates); b) shrinking U.S. growth premium (owing to negative supply shocks such as tariffs and reduced immigration); and c) diminished foreign demand for U.S. assets (from erosion of U.S. policy certainty and narrower U.S. trade deficits). **Given these dynamics, we suggest investors stay invested but diversify their portfolios by increasing exposure to International Equities alongside their core U.S. holdings.**

## U.S. Interest Rates

**Forecasts:** We continue to forecast a gradual decline in interest rates as the Fed attempts to manage a shifting inflation and growth mix in 2025–2026. **Specifically, our outlook calls for two rate cuts in 2025 and three more in 2026, unchanged from our prior view.** Notably, we are more dovish in the near term than current Fed guidance for two rate cuts this year and only one rate cut next year, but our estimate of the long-term ‘neutral’ rate of 3.375% remains above the Fed’s estimate of 3.0%. Key to our thinking is that the Fed will continue to outperform on its employment vs. inflation mandate, meaning a higher resting rate for inflation in equilibrium.

**At the long end of the curve, we have revised our 2025 10-Year Treasury yield forecast to 4.25–4.5%, up from 4.25%, while our 2026 forecast rises to 4.25%, up from 4.0% previously.** Top of mind to us is that term premium and inflation uncertainty will continue to weigh on bonds in the near-term. Longer term, we stick to our 4.0% forecast for UST yields, which we think is a fairly conservative base case relative to history.

**Exhibit 62: We Still See a Higher for Longer Interest Rate Environment, Except in China, Relative to Pre-COVID**

### KKR GMAA 10-Year Interest Rate Forecast and Probability, %

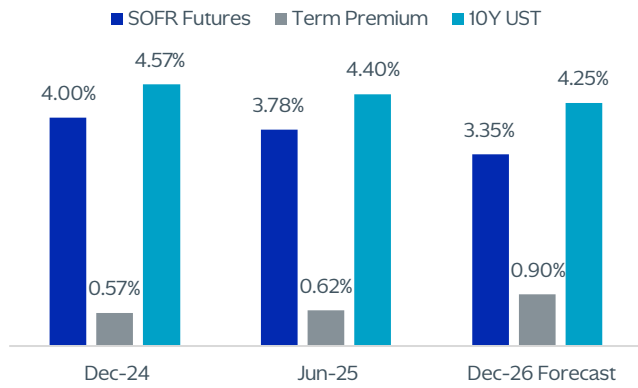
	Base	Low	High
<b>U.S.</b>	<b>60%</b>	<b>20%</b>	<b>20%</b>
2025e	4.25–4.5%	3.0%	5.25%
2026e	4.25%	3.0%	5.0%
<b>Euro Area</b>	<b>60%</b>	<b>20%</b>	<b>20%</b>
2025e	2.75%	1.6%	3.5%
2026e	3.0%	1.8%	3.7%
<b>China</b>	<b>55%</b>	<b>30%</b>	<b>15%</b>
2025e	1.5%	1.2%	1.8%
2026e	1.2%	0.9%	1.5%
<b>Japan</b>	<b>60%</b>	<b>20%</b>	<b>20%</b>
2025e	1.6%	1.2%	2.0%
2026e	1.8%	1.4%	2.2%

Data as at June 30, 2025. Source: KKR Global Macro & Asset Allocation analysisdai.



**Exhibit 63:** We See U.S. Term Premium Putting Upward Pressure on Rates

**U.S. 10-Year Treasury Decomposition and Forecasts**



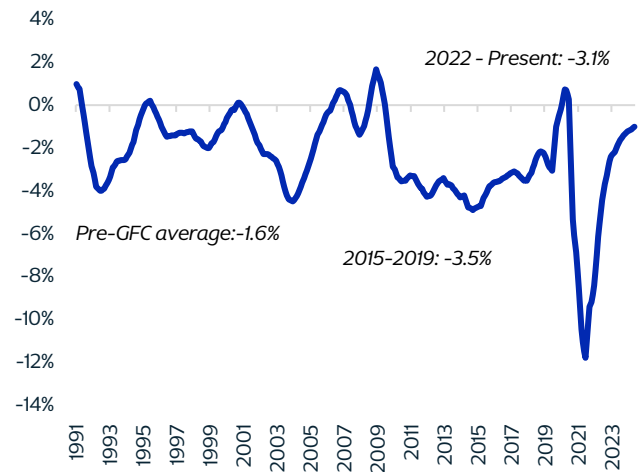
Data as at June 15, 2025. Source: Bloomberg, KKR Global Macro & Asset Allocation analysis.

**Commentary:** On the front end of the curve, we continue to think that the Fed wants to lower real rates, from current restrictive levels of around 2% (roughly in-line with the level of run-rate growth in the U.S.), back towards 1% (about 100 basis points below real growth). Indeed, our estimate for a ‘neutral’ setting of real rates relative to real growth would be consistent with the prevailing levels in the 1990s-2000s, but much more restrictive than the post-GFC era when real rates were routinely negative. One can see this in *Exhibit 64*.

We think the Fed’s latest dot-plot, which showed policymakers’ intention to cut rates twice this fall, even as tariffs put upward pressure on inflation and unemployment remains well below 5%, suggests that *Fed policymakers recognize that the cumulative impact of rate hikes this cycle is now becoming too high*. As such, our forecast shows real rates falling through mid-late 2026 towards around zero percent (as growth slows and the Fed seeks to provide more accommodation) before stabilizing at around 1% in the long run. In nominal terms, this corresponds to a fed funds rate of 3.875% in 2025, 3.125% in 2026, and 3.375% longer-term. One can see this progression in *Exhibit 65*.

**Exhibit 64:** We See Real Rates Settling Around 100 Basis Points Below Real GDP Growth, or Roughly Where They Were Pre-GFC

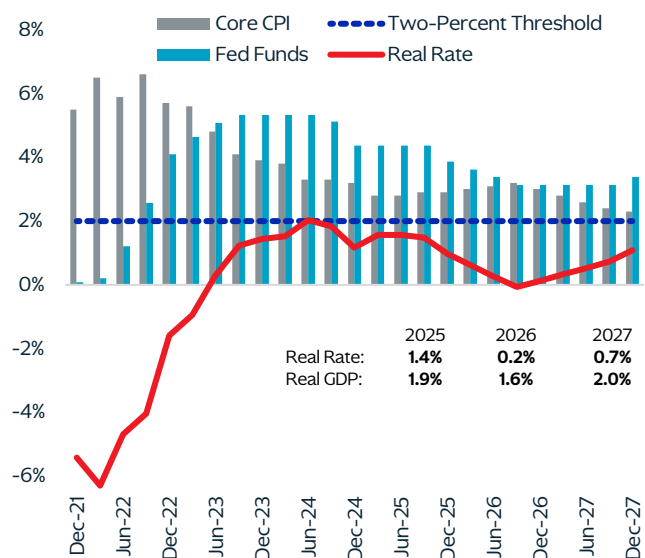
**Trailing Twelve Month Real Rate - Real GDP, %**



Data as at June 6, 2025. Source: Bloomberg, KKR Global Macro & Asset Allocation analysis.

**Exhibit 65:** Our View Means the Fed Needs to Reduce Real Rates from Currently Elevated Levels

**Fed Funds, CPI, and Real Rates, %**



Data as at June 6, 2025. Source: Bloomberg, KKR Global Macro & Asset Allocation analysis.

**Exhibit 66: Contrary to Popular Wisdom, There Are Actually Only A Few New Ambitious Spending Programs from the Administration at a Time When Tariff Revenue Is Climbing**

	2025	2026	2027	2028	2029
Current Law Deficit	1,915	1,779	1,746	1,973	2,001
Preventing Tax Hikes (Indiv/Corp/Estate)	7	191	369	387	394
Border Security & Defense Funding	2	49	57	47	48
New Changes TCJA Structure + SALT	15	89	78	82	68
Restoring TCJA Capex Provisions (5 Years)	55	128	102	84	58
IRA Reforms	0	-13	-40	-45	-60
Full Expensing for Mfg Structures	2	30	35	34	29
Trump's Campaign Promises	9	94	90	92	51
E&C Health Spending Cuts	-1	-25	-38	-50	-92
Ed & Workforce Cuts	-17	-31	-31	-31	-34
Agriculture Spending Cuts	0	-12	-16	-30	-30
All Other (Including Judiciary Revenues)	-1	-7	-19	-27	-33
Other Tax Offsets	-14	-44	-61	-66	-62
Other Tax Cuts	2	11	13	17	17
Increase in Spending	59	460	539	494	354
Impact on Debt Service	1	11	29	48	64
Tariff Revenue	-25	-260	-280	-280	-280
Total Increase in Deficit	35	191	288	262	138
Total Deficit	1,950	1,970	2,034	2,235	2,139
Deficit as % of GDP	6.5%	6.3%	6.3%	6.6%	6.1%

Estimates consistent with a ~15% tariff rate on 2.5 trillion goods, at a 75% multiplier. For conservatism, deficit growth is based on run-rate 4% NGDP growth. Data as at May 31, 2025. Source: PSC, Bloomberg, KKR Global Macro & Asset Allocation analysis.

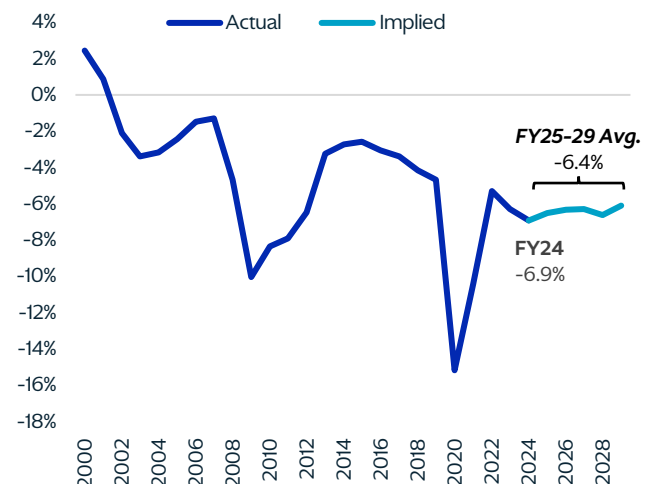
For bond yields, we take market concerns about wide deficits seriously. We also continue to think that a disruption of trade flows from tariffs will weigh on foreign appetite to buy USTs, particularly in the near term, as there will be fewer dollars to recycle back into government debt. As such, we do not discount the possibility of *near-term* volatility in bond yields. Ultimately, though, we see important offsets that mean the sustainable range for bond yields is closer to 4% than 5%.

Key to our thinking is that Treasury supply is likely stabilizing, albeit at high levels. Moreover, we would emphasize that historical experience in most countries has been that government deleveraging actually entails lower bond yields, a steeper yield curve, and a weaker currency, and as such, we think the current fiscal risks are more of a challenge to the USD than to the 10-Year Treasury. Meanwhile, we continue to think that foreign buying can be offset by the Fed through both interest rate and balance sheet policy, while the outlook for household demand is relatively stable.

Let's start with the deficit picture. As we have predicted for some time, there has been no material deficit expansion from the current administration. Indeed, the total sum of President Trump's *new* campaign promises is likely less than 100 billion/year, compared to an approximate 400 billion per year cost associated with extending the TCJA from his first administration (which will not change the government's fiscal stance). On the revenue side, the silver lining from tariffs sticking at higher levels is that there will be a likely *offset* of 250-300 billion per year from tariff revenue, which will help offset new spending. All told, we think these factors will be enough to keep the deficit closer to 6% than 7% in coming years, meaning UST supply is unlikely to surge.

**Exhibit 67: We Think Deficits Settle Closer to 6% than 7% in Coming Years**

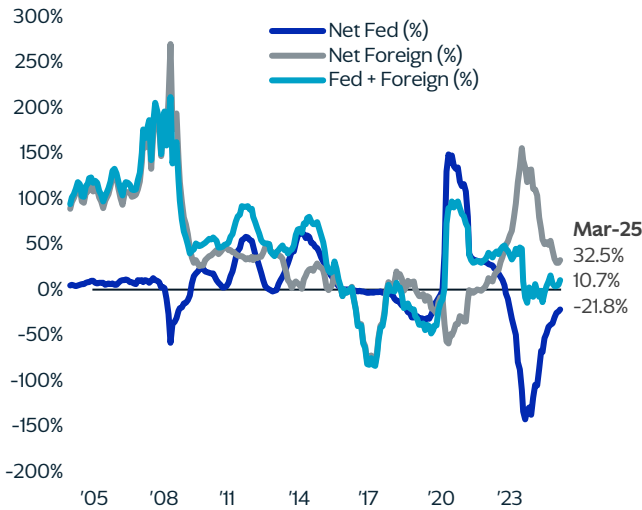
**U.S. Deficit, as a % of GDP**



Data as at May 31, 2025. Source: PSC, Bloomberg, KKR Global Macro & Asset Allocation analysis.

**Exhibit 68: Ending Fed QT Can Help Offset About 2/3rds of Recent Foreign Demand Were It to Slow**

**Fed and Foreign Share of Total U.S. Long-Term Debt Issuance (L12M)**



Data as at March 31, 2025. Source: Bloomberg, KKR Global Macro & Asset Allocation analysis.

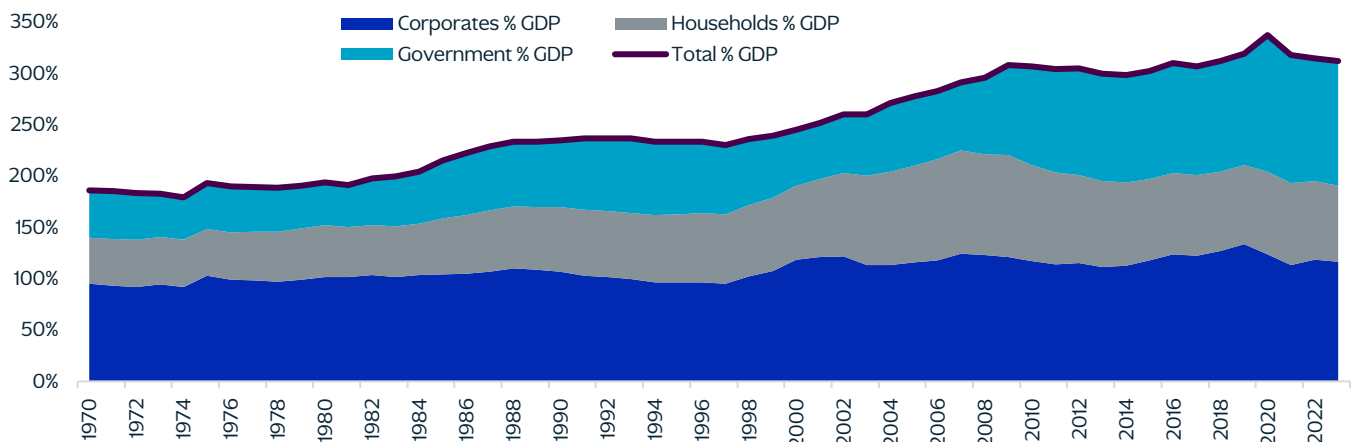
Meanwhile, on the demand side of the equation, we think markets have not fully appreciated the impact of the Fed migrating from quantitative tightening to a neutral balance sheet policy. See *Exhibit 68*, but we estimate that this shift can make up for about two-thirds of net current foreign de-

mand were it to slow. In addition, we continue to think that a weaker USD means that the cost of hedging is becoming a more important input into U.S. bond yields. Specifically (and all else being equal), our math suggests that hedged UST yields are about 50 basis points from levels that will attract more Japan and Europe buyers, which should help keep a cap on yields in the near term (*Exhibit 71*), though we do think the benefit will lessen over time if we are right that Japan and Europe yields rise from here. While these factors would not offset disorderly foreign selling of Treasuries, they should help replace lackluster foreign demand.

We also want to remind folks that government borrowing represents a relatively small share of total U.S. debt. Indeed, our math in *Exhibit 69* shows that total U.S. borrowing has remained relatively constant compared to GDP, as households have deleveraged while government deficits have grown. We think many of these same households will be incentivized to buy USTs at current yields, even if we are right that treasuries are a less effective hedge in investor portfolios this cycle. We can see in *Exhibit 69* that households are incentivized to put savings into government debt vs. corporate debt, even at current elevated levels of stock-bond correlation, so long as 10-Year yields are no more than 300-400 basis points below the yield on HY debt (currently, we are at 300 basis points, suggesting households are incentivized to buy USTs).

**Exhibit 69: Because of Corporate and Consumer Deleveraging, Total Leverage Has Been Relatively Stable in the U.S., Even as Government Debt Has Grown**

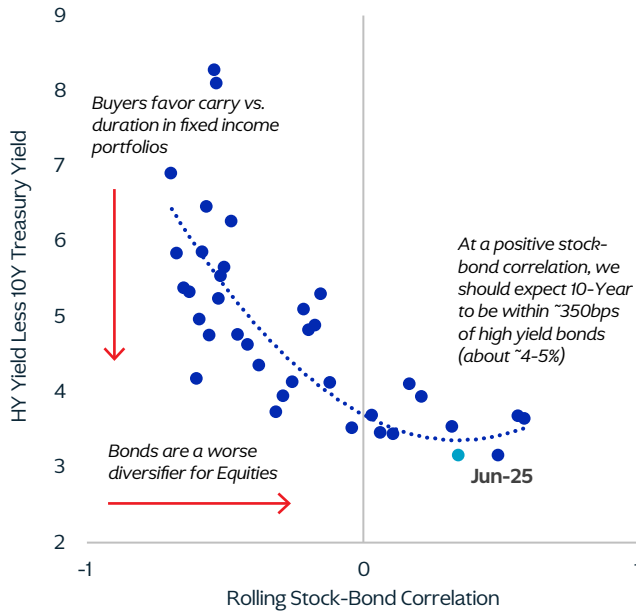
**Debt to GDP Ratio by Sector, %**



Data as at December 31, 2024. Source: Haver Analytics, U.S. Bureau of Economic Analysis, KKR Global Macro & Asset Allocation analysis.

**Exhibit 70: We Think Households Are Incentivized to Hold USTs at Current Yields, Despite Diminished Hedging Benefit**

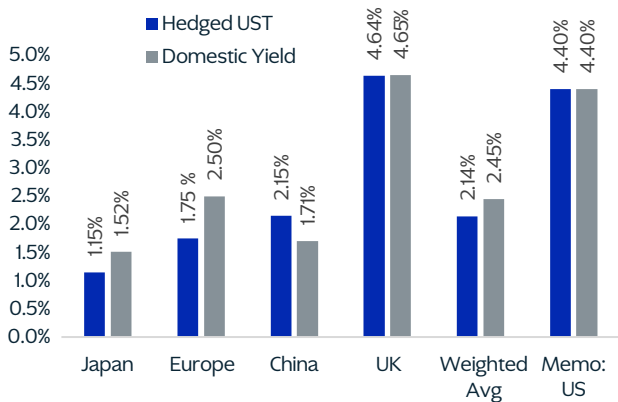
**Stock-Bond Correlation vs. Excess Treasury Yield**



Based on rolling 3-Year quarterly correlation. Data bucketed in 2.5%ile ranges, with top/bottom 5%ile excluded as outliers. Data as at June 6, 2025. Source: Bloomberg, KKR Global Macro & Asset Allocation analysis.

**Exhibit 71: Despite Elevated Hedging Costs, UST Yields Now Appear Near Levels That Would Attract More Japan, European Investors**

**Domestic Yield vs. Hedged UST Yield by Market, %**



Uses 2-Year hedge costs. Data as at May 30, 2025. Source: Bloomberg, KKR Global Macro & Asset Allocation analysis.

With all of that said, we have often been asked: what if you are wrong about the deficit picture, and the U.S. government is forced to lower leverage in order to placate ‘bond vigilantes’? To answer that question, we looked at what occurred during three historical episodes where governments borrowed too much and were forced to deleverage: Belgium in the 1990s, Canada in the 1990s, and the Eurozone following the GFC. In each case, we looked at the 10-year period that coincided with a peak in government debt / GDP levels. We also looked at Japan in the lead-up to the GFC, which showed a scenario for expanding government deficits paired with sluggish real growth.

Interestingly, in all these cycles, 10-year bond yields tended to fall over time, as fiscal tightening was offset by aggressive monetary easing. One can see this in Exhibit 72. So, while yield curves often settled at steeper levels in these scenarios (and bond yields did tend to pick up on a quarter-to-quarter basis), lower overall rates meant that bond yields did not become unglued on a sustained, year-to-year basis. In fact, our observation is that investor discomfort with wide deficits tends to be expressed through currency weakness rather than a big surge in government bond yields.

Moreover, we would emphasize that historical experience in most countries has been that government deleveraging actually entails lower bond yields, a steeper yield curve, and a weaker currency, as such, we think the current fiscal risks are more of a challenge to the USD than to the 10-year Treasury.

**Exhibit 72: High Levels of Government Debt Tend to Lead to Weaker Currencies, But Not Necessarily Always Higher Bond Yields**

Major Government Deleveraging Cycles					
		Belgium	Canada	Eurozone	Memo: Japan
Dates	Start	1990	1991	2007	1996
	End	2000	2001	2017	2006
Government Debt/GDP	Start	104%	56%	66%	66%
	Peak	117%	65%	93%	—
	End	99%	46%	88%	133%
Currency	Start	0.0%	0.0%	0.0%	0.0%
	Trough	-33.3%	-28.2%	-26.4%	-19.3%
	End	-33.3%	-28.2%	-18.7%	-4.1%
10-Year	Start	10.0%	8.1%	4.3%	2.8%
	Peak	10.0%	9.1%	4.3%	2.8%
	End	5.6%	5.4%	0.4%	1.7%
2-Year	Start	10.1%	7.0%	4.0%	0.7%
	Peak	10.1%	8.6%	4.0%	0.8%
	End	5.0%	3.2%	-0.6%	0.8%
10s/2s	Start	-0.1%	1.1%	0.3%	2.1%
	Peak	2.6%	2.3%	2.1%	2.1%
	End	0.6%	2.2%	1.1%	0.9%

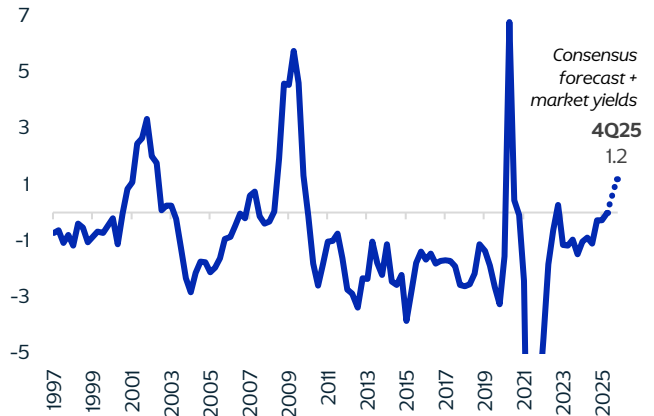
For Belgium, Canada, and Eurozone, data reflects 10-Year period with 'peak' government debt/GDP occurring in year five. For Japan, data represents 10-Year period of debt growth prior to GFC. Data as at June 30, 2025. Source: Haver Analytics, IMF, Federal Reserve Board, Bloomberg.

No doubt, we do not mean to suggest all is well. From the examples above, we are cognizant that bond vigilantes could drive U.S. yields to uncomfortably high levels on a temporary basis before fiscal restraint emerges. Rather, our view is that these moves are unlikely to sustain bond yields at high levels, particularly given that real yields are already too high across the yield curve and need to come down.

So, pulling it all together, what is our call? Our best estimate is that term premium needs to rise to accommodate worsening fundamentals, which means that bond yields will not rally much as rates fall and that the currency will continue to weaken (Exhibit 74). However, we do not expect 10-Year yields to become unglued on a sustainable basis the way some investors fear.

**Exhibit 73: We Don't Think Real Growth Can Support Treasury Yields at Current Levels for Too Long. As Such, Our Work Suggests That a Low-Four Percent Range Yield Ultimately Prevails**

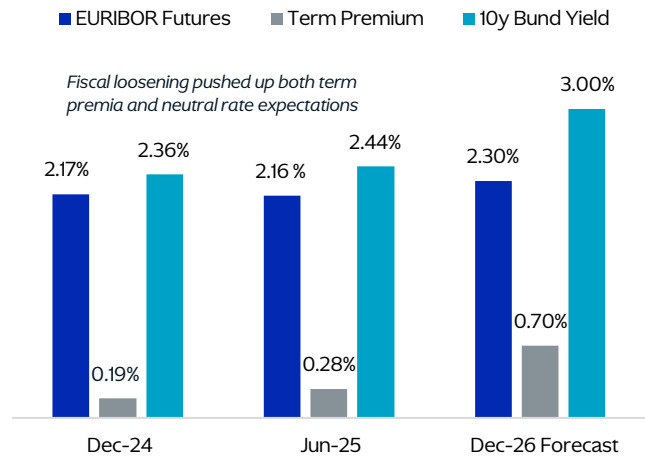
**TIPS Yield vs. Real GDP Growth**



4Q25 based on market TIPS yields + consensus 4Q Y/y GDP forecast. Data as at May 30, 2025. Source: Bloomberg, KKR Global Macro & Asset Allocation analysis.

**Exhibit 74: Rising Term Premium Is Not Just a U.S. Phenomenon. We See It as a Structural Factor in a World with More Outstanding Government Debt**

**10-Year Bund Yield Decomposition and Forecasts**



Data as at June 15, 2025. Source: Bloomberg.



**Where to be on the curve?** We continue to suggest patience, discipline, and duration neutrality until there is greater clarity on inflation, fiscal direction, and the end state of Fed policy. While we do see the U.S. dollar weakening, the robust technical picture leads us to believe that the long end of the curve will not get unglued the way some market pundits have been signaling. This view is important to our more optimistic outlook, as is our base case that Middle East tensions do not unravel the transportation of commodity flows. That said, for investors, our longer-term thesis remains ‘this time is different’. Specifically, we do see the correlation between stocks and bonds remaining positive, compared to its prior role as negatively correlated prior to the pandemic (a period when bonds could serve as important shock-absorbers in a diversified portfolio). So, as we describe more below in Section IV, Frequently Asked Questions, we think an investor must approach asset allocation differently this cycle, including owning more operational improvement stories, more upfront yield, and more non-correlated assets.

**Bottom Line:** The Fed is not finished, but it is increasingly deliberate. A slow descent in policy rates, coupled with sticky term premiums, defines our near-term rates outlook. With real rates already highly restrictive by historical standards, we see limited room for the Fed to hold higher for longer without further damage to rate-sensitive sectors. While the Fed is maintaining optionality, we believe additional easing will be needed in 2026 to avoid a rise in defaults and preserve credit health.

## Euro Area Interest Rates

### Forecasts

In our base case, we expect the ECB to cut its deposit rate once more this year to 1.75% (in line with consensus) as inflation pressures subside and the region continues to grapple with the uncertainty from trade policy. From there, we believe policy will move towards 2.25% (our estimate or neutral) by year end-2026, compared to consensus of 1.75%. Meanwhile, on the long-end of the curve, we retain our above-consensus view on long-end rates. Specifically, we forecast the 10-Year bund yield rising to 2.75% at end-2025 and 3.0% in 2026 (vs. consensus of 2.65% and 2.8% in 2025 and 2026, respectively), reflecting the repricing of term premia and more fiscal spending.

### Commentary

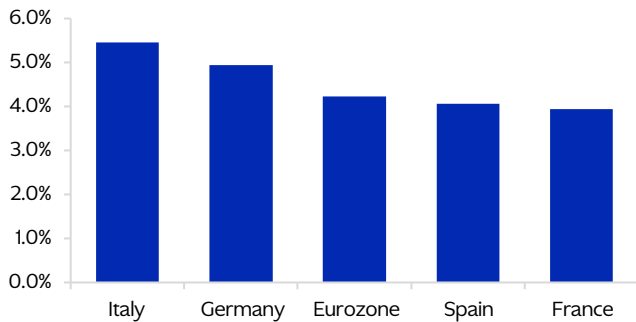
Headline inflation is now broadly in line with the ECB’s target, and medium-term inflation expectations have re-anchored across both market-based and survey measures. Importantly, real policy rates, previously firmly in restrictive territory, have now moved close to zero, reflecting a substantial shift in the monetary stance. This development is significant: as the drag from tight policy fades, credit conditions are beginning to ease, supporting lending activity and broader economic normalization. The Euro Area is thus entering a phase in which monetary policy is no longer acting as a brake on growth, in contrast to the U.S., where real rates remain materially positive, and policy is expected to stay restrictive for longer.

Turning to sovereign bond markets, historical experience suggests that rising bund yields have often triggered widening in periphery spreads, particularly in more indebted sovereigns. However, this time around, spreads have remained remarkably tight. In fact, despite ongoing ECB balance sheet reduction and higher core yields, spreads have narrowed, not widened. Notably, Italian BTP-Bund spreads have closed to just 98 basis points (as of June 20, 2025) and are close to all-time lows. This resilience is supported by a combination of stronger domestic fundamentals, improved fiscal credibility in some periphery countries, and strong domestic and foreign demand for sovereign paper.

A slow descent in policy rates, coupled with sticky term premiums, defines our near-term rates outlook. With real rates already highly restrictive by historical standards, we see limited room for the Fed to hold higher for longer without further damage to rate sensitive sectors.

**Exhibit 75:** Despite Significant QT Italian BTP and German Bund Spreads Are at the Tightest in 15 Years as Households and Foreigners Have Stepped Up Buying

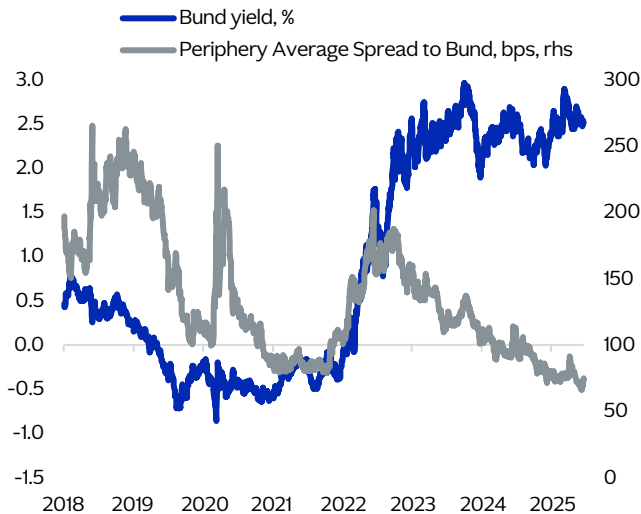
**ECB QT: Net Sales of Government Debt Since July 22, % of GDP**



Data as at April 30, 2025. Source: ECB.

**Exhibit 76:** Periphery Spreads Have Historically Blown Out With Rising Yields but Faster Growth Momentum Resulted in Periphery Spreads Tightening to Close to All-Time Lows

**Bund Yield vs. Periphery Spreads**



Periphery spreads are average of Italy, Greece, Spain and Portugal 10-Year to Germany. Data as at June 20, 2025. Source: Bloomberg.

Relative to consensus, our 2025-26 oil forecasts are modestly below futures pricing.

## Oil

**Forecasts:** We remain cautious on oil prices, as the diminishing geopolitical risk premium brings the bearish fundamental backdrop back into focus. Specifically, we expect the oil market to move into larger surpluses over the next six to 12 months, driving WTI oil prices back down to \$60 per barrel on average in the second half of 2025 and 2026. Relative to consensus, our 2025-26 forecasts are modestly below futures pricing, but our medium-term 2027-28 forecasts of \$65-70 per barrel remain above futures at approximately \$63 per barrel (*Exhibit 77*).

**Exhibit 77:** We Expect WTI Oil Prices to Average Roughly \$60 Per Barrel in the Second Half of 2025 and 2026, Which is Modestly Below Futures Pricing of \$62-65 Per Barrel

**KKR GMAA Oil Price Forecasts, US\$**

	GMAA Base Case vs. Futures			High/Low Scenarios		Memo: Apr-25 Forecasts	
	KKR GMAA	WTI Futures	KKR GMAA vs. Futures	KKR GMAA	KKR GMAA	KKR GMAA	WTI Futures
	June 2025			High Case	Low Case	April 2025	
2021a	68	68	n/a	68	68	68	68
2022a	95	95	n/a	95	95	95	95
2023a	78	78	n/a	78	78	78	78
2024a	76	76	n/a	76	76	76	76
2H25e	60	65	-5	85	50	60	64
2026e	60	62	-2	85	50	60	60
2027e	65	62	3	95	55	65	61
2028e	70	63	7	95	60	70	61

Forecasts represent full-year average price expectations. Latest forecasts as at June 26, 2025. Prior as at April 23, 2025. Source: Bloomberg, KKR Global Macro & Asset Allocation analysis.

**Commentary:** We see larger inventory builds to the tune of approximately 1.0 million barrels per day on average over the next few quarters as supply growth outpaces global demand

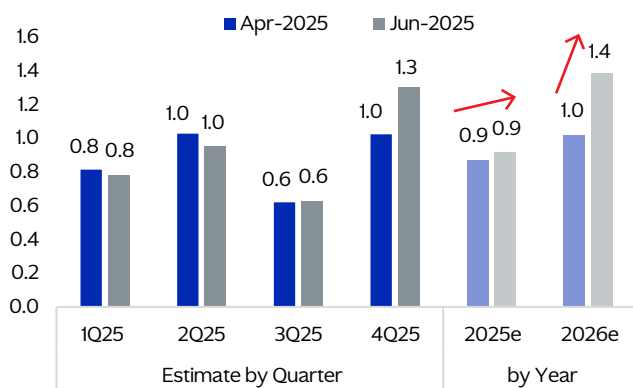
- **Subdued Global Demand:** Given our tepid outlook for global GDP growth, we expect global oil demand to rise by just 1.0 million barrels per day this year and 0.8 million barrels per day next year. For context, these

figures are below the long-term median growth rate of 1.3 million barrels per day and are more in-line with the pace seen during the 2001 downturn.

- Shift in OPEC+ Strategy:** Saudi Arabia is once again prioritizing volume over price, in our view. While we do not envision a repeat of the sharp, all-out price war seen in 2014 and 2020, the kingdom is now focused on normalizing spare capacity, maintaining internal cohesion, and reclaiming market share from both U.S. shale and other OPEC+ members. As such, supply growth from OPEC+ alone is likely to outpace total oil demand growth this year.
- Other Supply Tailwinds:** We expect supply growth from the Americas to continue, driven by both the U.S. and Canada, as well as the price-inelastic production increases in Brazil and Guyana. In the U.S., the recent oil price rally likely enabled shale producers to lock in favorable forward prices, which could support higher production into 2026. Preliminary data also show Iranian oil output ironically at a seven-year high (over 3.5 million barrels per day). Given President Trump’s sensitivity to high oil prices, stricter sanctions on Iran now appear less likely after the recent ‘12-Day War’ with Israel.

**Exhibit 78:** Oil Markets Are Poised for Larger Inventory Builds in 2025 and 2026, as Supply Growth Outpaces Global Demand

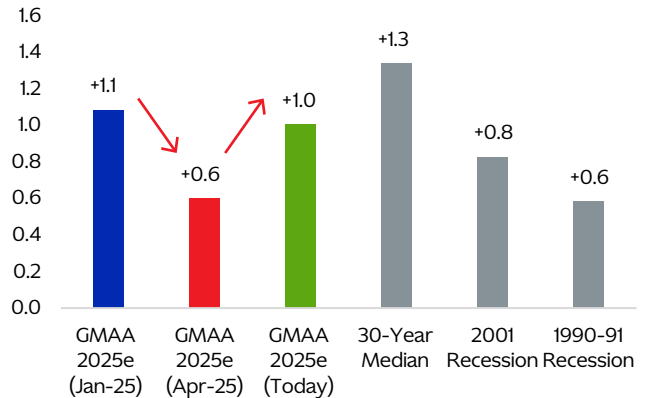
**Global Supply Surplus/Deficit, Millions of Barrels per Day Consensus Estimates**



Consensus includes MS, JPM, S&P Global, UBS, Piper Sandler, GS, and RBC. Data as at June 26, 2025. Source: Broker Research, KKR Global Macro & Asset Allocation analysis.

**Exhibit 79:** We Expect Subdued Global Oil Demand Growth of 1.0 Million Barrels per Day This Year and 0.8 Million Barrels per Day in 2026

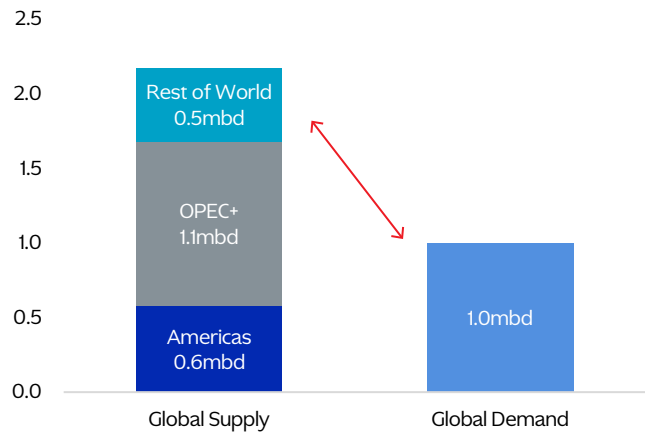
**Global Oil Demand Growth, Millions of Barrels per Day**



Data as at June 26, 2025. Source: Haver Analytics, Energy Intelligence, IEA, KKR Global Macro & Asset Allocation analysis.

**Exhibit 80:** Global Oil Supply This Year Should Handily Beat Global Oil Demand. In Fact, OPEC+ Production Alone Could Surpass the Total Incremental Demand

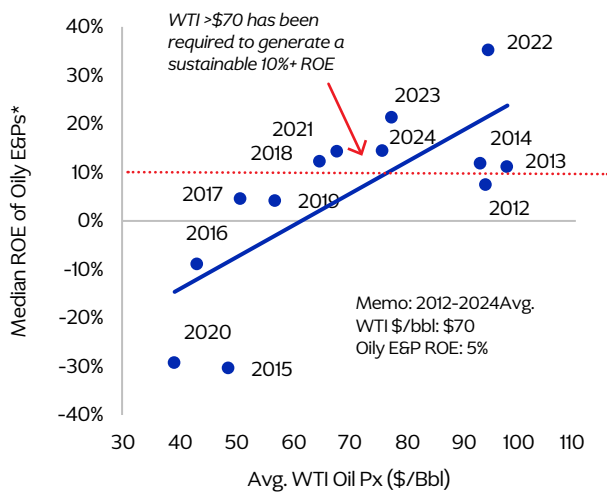
**2025e Global Supply vs. Global Demand Growth, Millions of Barrels per Day**



Data as at June 26, 2025. Source: Haver Analytics, Energy Intelligence, KKR Global Macro & Asset Allocation analysis.

**Exhibit 81: In a World Where Shale Producers Are Disciplined About Return on Capital, We Still Think WTI Prices Are Likely to Average >\$70 Over the Longer Term**

**Median ROE of Oily E&Ps vs. Avg. WTI Price**



\*Median of COP, EOG, PXD, OXY, FANG, APA, PDCE, MGY, MUR, DEN, CIVI, CRC, SM, CDEV, TALO. Data as at June 26, 2025. Source: Bloomberg, KKR Global Macro & Asset Allocation analysis.

Overall, we continue to expect a challenging and oversupplied oil market through the second half of 2025 and into 2026. Unless there is a renewed geopolitical flare-up, headwinds such as tariffs, weaker global demand, and a shift in Saudi Arabia’s market management strategy are likely to prolong the supply glut and delay any recovery in oil prices.

However, we remain more constructive on the medium-term outlook for crude oil. Key to our thinking are the upward pressures emanating from unsettled geopolitics, an at-times messy energy transition, lower oil prices for longer crowding-out supply and boosting demand, and the structurally higher ROIC discipline we are seeing from OPEC and non-OPEC producers alike.

## U.S. Dollar

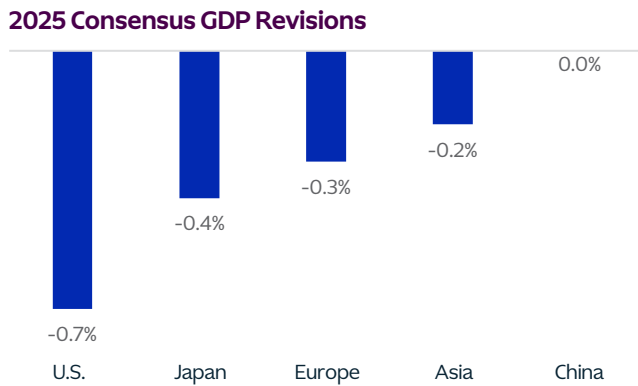
**Forecast:** Our analysis shows that the dollar is currently overvalued by roughly 15-20%, placing it near some of the highest levels seen in recent history. We remain convinced that the macro environment is bearish for the dollar, both from a cyclical and a structural standpoint. On the cyclical side, the growth differential has shifted away from the U.S., favoring other regions. Structurally, the dollar has

diverged significantly from what real rates would suggest, indicating that its recent weakness is not just due to short-term cyclical factors but likely reflects deeper, longer-term trends.

**Commentary:** While we do not expect a wholesale exit from dollar assets—given the size and liquidity of U.S. capital markets—it is important to recognize how these cyclical and structural pressures are playing out within a context of historically high valuations. From a cyclical perspective, relative growth differentials have moved away from the U.S. in favor of the rest of the world. Consider that consensus GDP growth expectations have fallen nearly -0.7% in the U.S. since the beginning of the year compared to a -0.4% downgrade in Japan and -0.3% in Europe. In other words, the narrative of U.S. exceptionalism, which has been a defining characteristic of the global economy this cycle, is reversing. From a structural perspective, the dollar has meaningfully diverged from what real rates would imply, which suggests the recent weakness extends beyond short-term cyclical pressures. Notably, the dollar began to sharply diverge from rate differentials after ‘Liberation Day,’ a period that coincided with heightened trade-related policy uncertainty. This dollar selloff also occurred alongside declines in stock and bond markets, which is unusual given the dollar’s traditional role as a safe haven. To us, this divergence hints at early signs of a potential reallocation away from dollar-denominated assets.

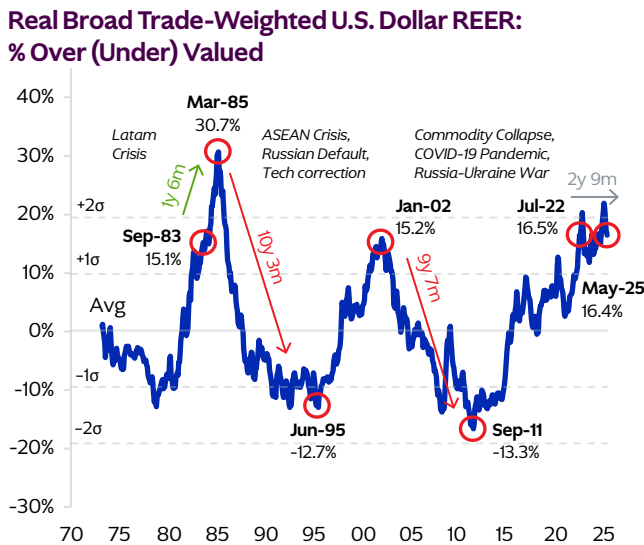
Since 1970, when Fed data begins, only two periods stand out when the trade-weighted dollar was overvalued by 15% or more: once in the mid-1980s and again in the early 2000s. The first instance, in September 1983, saw the dollar appreciate further for about 1.5 years before entering a decade-long bear market triggered by the Plaza Accord. Similarly, in February 2002, the dollar peaked just above a 15% overvaluation, marking the start of another roughly 10-year decline, eventually slipping around 13% below fair value. What makes today different is that since hitting the +15% overvaluation mark in early 2022, the dollar has been oscillating within a volatile range for nearly three years.

**Exhibit 82:** The U.S. Versus the Rest of World Growth Differential Is Falling



Data as at June 30, 2025. Source: Bloomberg.

**Exhibit 83:** This Is the Longest Stretch Since the 1970s Where the Dollar Has Sustained >15% Overvaluation On a REER Basis. We Think This Pattern Could Change More Heading Into 2026



Data as at June 30, 2025. Source: Bloomberg.

History suggests that in the near term; capital inflows can continue to support the dollar—much like in the 1980s and relative to some Asian currencies where USD valuations remain stretched. However, our broader outlook aligns more with the early 2000s scenario. We believe we are nearing the end of a period characterized by outsized U.S. returns, large equity inflows, and a dominant share of global portfolios allocated to U.S. assets. That said, there are notable differences today—such as oil not being in a bull market as it was in the 2000s, and Chinese growth not being as robust, factors that helped accelerate the USD decline back then.

While we do not expect a rapid or steep drop like that in the early 2000s history indicates that the dollar is likely to eventually revert to trading at a discount on a real effective exchange rate basis—possibly below ‘par’—over the next decade or so.

Structurally, the dollar has diverged significantly from what real rates would suggest, indicating that its recent weakness is not just due to short-term cyclical factors but likely reflects deeper, longer-term trends.



## SECTION IV

# Frequently Asked Questions

## QUESTION NO. 1

### What could Europe do to improve its competitive positioning?

As we spend time with global investors post ‘Liberation Day’, Europe consistently emerges as a region that could see significant benefits if allocations shift away from the United States towards other markets. However, Europe’s track record remains sluggish as regulation and demographics continue to constrain productivity growth below trend, especially when compared to the U.S.

With this in mind, we collaborated with Aidan Corcoran and his team—Bola Okunade and Asim Ali—to identify three key changes (in addition to cheaper energy costs which we have been highlighting for some time through our Climate/Infrastructure efforts, given that traditional costs are 50%+ higher than in other markets like the U.S.)—we believe could help turn the tide and enhance Europe’s growth prospects. They are as follows:

**1. The Euro as a Reserve Currency:** Today, the euro accounts for around 20% of global FX reserves, a share that has barely moved in over a decade. In contrast, the U.S. dollar still commands nearly 60% of reserves worldwide. This imbalance matters because the demand for dollar-denominated assets has long given the U.S. a structural advantage—keeping interest rates lower, easing the cost of capital, and fueling investment-led growth across the economy. For Europe to compete, we think it needs to change the equation.

That would start with accelerating the Capital Markets Union (CMU), a long-standing initiative that, if fully realized, could dramatically improve the depth, liquidity, and integration of European financial markets. Today’s fragmented regulatory landscape, shallow corporate bond markets, and limited scale in equity financing are clear bottlenecks to euro-based capital formation. Without progress here, the euro will remain a currency of trade, not a true reserve anchor.

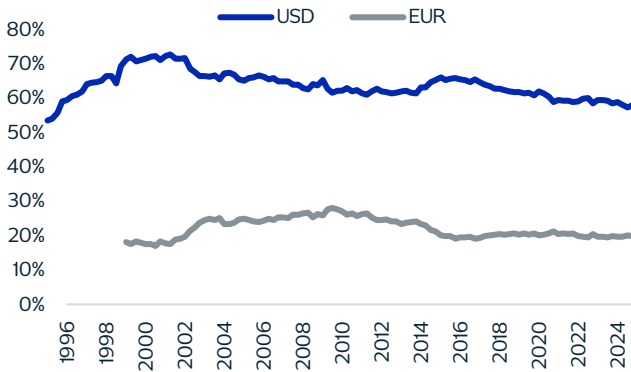
Yet, the opportunity is there. If Europe can remove internal frictions—harmonizing disclosure rules, easing cross-border investment, and promoting scale in public and private capital markets—it could reposition the euro as a credible store of value for global reserves. That shift would carry real macro benefits: increased demand for European assets, lower sovereign and corporate funding costs, and a stronger foundation for long-term growth.

The key, then, in our view, to improving Europe’s competitiveness is to focus on building the financial infrastructure to attract and retain global capital and better compete with the U.S. dollar, not subsidies or reindustrialization.

Today, the euro accounts for around 20% of global FX reserves, a share that has barely moved in over a decade.

**Exhibit 84:** The Euro Remains the World’s Second Most Important Reserve Currency, But It Continues to Trail the Dollar by a Wide Margin

**Official Foreign Exchange Reserves, % of Allocated Reserves**



Data as at December 31, 2024. Source: IMF.

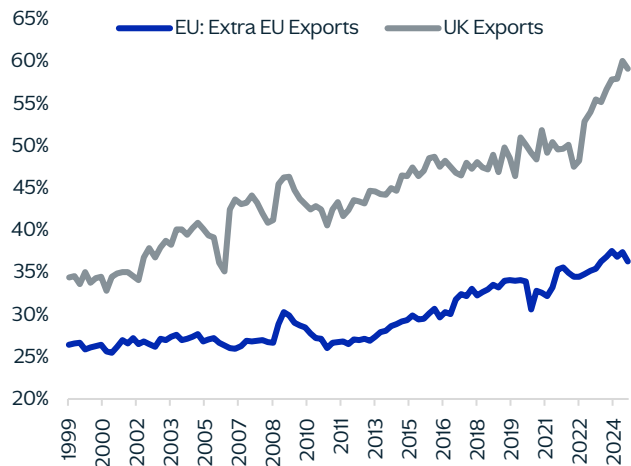
**2. Cross-border Services and IT Market Share:** At a time when tariffs and global fragmentation are reshaping the macro landscape, we believe Europe may finally be entering a phase of self-correction—one that could unlock real upside for investors, particularly in services. For too long, Europe’s Single Market has been more ambition than reality, especially when it comes to services integration. Barriers between EU member states, that are effectively ‘internal tariffs’ equivalent to 110% for services have suppressed the region’s growth potential. However, with U.S. trade policy turning more adversarial and capital beginning to rotate away from U.S. assets, the strategic urgency in Europe is shifting.

What are we watching? Most importantly, we’re watching a serious push backed by leaders like Macron and von der Leyen to restore the original vision of the Single Market. That means streamlining licensing, reducing administrative friction, and enabling professionals, SMEs, and tech platforms to operate seamlessly across borders. If implemented, the impact on European services productivity, labor mobility, and capital deployment could be transformative, in our view. At KKR, this matters. It speaks to real investable change in Europe’s services ecosystem including digital platforms, professional services, regulated industries which are now seeing a surge in digitalization and energy transition investments, or the broader fintech and infrastructure stack that can

enable cross-border scale. It is also happening at a time when valuation differentials between U.S. and European Equities are near historic extremes and when we’re seeing evidence of capital rotation back into European markets. In short, we are not betting on convergence; rather, we are investing behind the policy urgency and institutional resolve that is starting to shift the center of gravity within the region’s economy.

**Exhibit 85:** Cross-Border Taxes Within the EU Are Keeping Europe’s Services Industry From Growing. By Comparison, the U.K. Have Been Much More Thoughtful in This Area Since Brexit

**Services Exports as a % Total Exports**

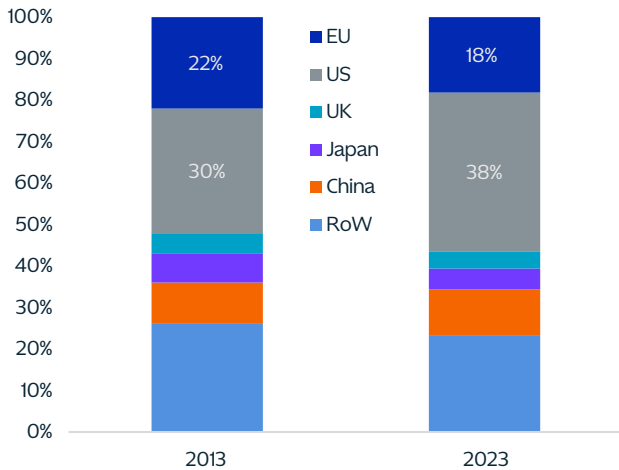


Data as at March 31, 2025. Source: Eurostat, ONS.

At a time when tariffs and global fragmentation are reshaping the macro landscape, we believe Europe may finally be entering a phase of self-correction—one that could unlock real upside for investors, particularly in services.

**Exhibit 86:** Between 2013 and 2023, the EU's Share of Global IT Revenues Declined From 22% to 18%, While the U.S.'s Share Rose a Full 8% Points From 30% to 38%

**IT Global Market Share by Geographic Area, %**



Data as at December 31, 2024. Source: IDC, Draghi Report.

**3. The Need for a Securitization Renaissance:** Europe's securitization market has been effectively frozen for over a decade—not for lack of need, but because of policy choices that have made securitized finance structurally uncompetitive. Regulatory overreach on both the supply and demand sides has suffocated the market: originators face higher capital charges and risk weights under the EU's 'non-neutrality' principle, while institutional investors—especially insurers—are constrained by punitive Solvency II capital requirements. The result? European insurers hold just 0.33% of their assets in securitized products, compared to 17% in the U.S. That delta represents a measure of how far behind Europe has fallen in capital efficiency.

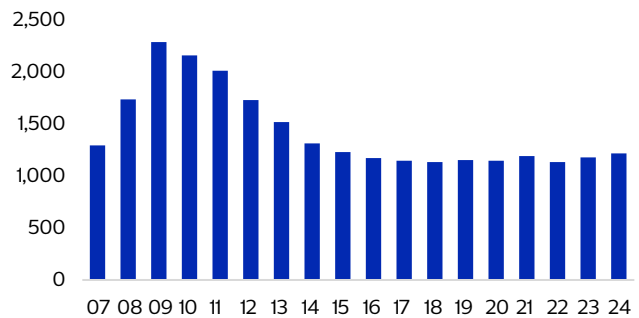
This matters because securitization is not about financial engineering. Rather, it is about unlocking balance sheet capacity and democratizing credit risk across the financial system. A reactivated securitization market would help move risk off bank balance sheets and expand access to capital across SMEs, Infrastructure, housing, and consumer credit. If Europe could raise its GDP share of true-sale securitizations to U.S. levels, it would generate an estimated €900 billion in incremental financing annually—a meaningful injection of credit dispersion at a time when the European banking system remains highly concentrated.

To their credit, policymakers are starting to acknowledge the misalignment. The European Commission has flagged the current treatment of securitized assets as overly restrictive, and reforms are under consideration to rebalance risk weights, improve transparency, and enhance market functioning. However, the imperative is broader than regulation. We believe Europe needs a functioning securitization market to reignite private credit formation, deepen capital markets, and close the competitiveness gap with the U.S.

In our view, a securitization renaissance is a necessary component of Capital Markets Union—a real lever for growth, credit transmission, and systemic flexibility. If Europe wants the euro to be a global reserve asset and its economy to be more than bank-financed, we think it is time to implement the necessary frameworks.

**Exhibit 87:** The Total European Securitization Market Has Held Flat at €1.2 Trillion for Nearly a Decade

**Outstanding European Securitisation Volumes, EUR Billions**

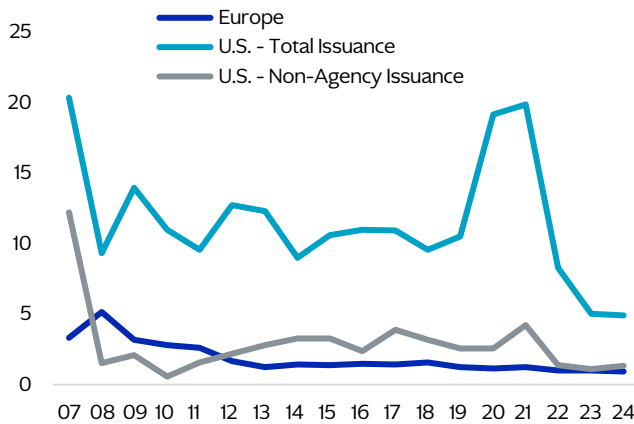


Data as at December 31, 2024. Source: AFME, Deutsche Bank Research.

A reactivated securitization market in Europe would help move risk off bank balance sheets and expand access to capital across SMEs, Infrastructure, housing, and consumer credit.

**Exhibit 88:** Relative to the Size of the Economy, Securitization Has Been a Much Bigger Force in the U.S. Relative to Europe (Partially as a Result of Government Guarantees)

**True-sale Securitisation Issuance as a % of GDP**



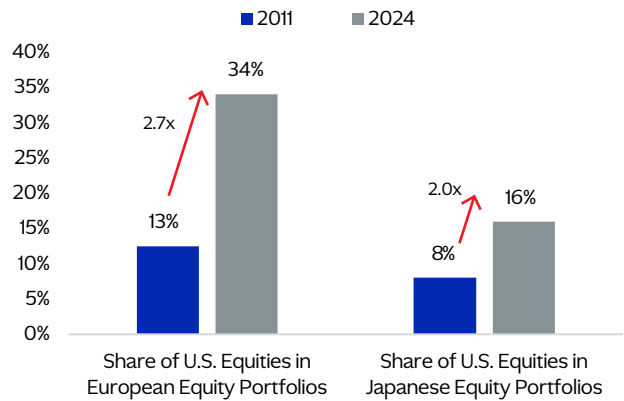
Data as at December 31, 2024. Source: AFME, Fed, Eurostat, Deutsche Bank Research.

Our bottom line: As investors are looking for new homes for their capital, Europe likely needs to do more—and more quickly—to make itself great again. Europe’s competitiveness challenge isn’t just about closing growth gaps; it’s about building institutional architecture to attract and retain global capital. We believe that starts with finishing what it started in fully realizing the Single Market for services, re-igniting securitization as a core engine of Private Credit formation and accelerating the Capital Markets Union to give the euro real reserve currency credibility. The good news is that the opportunity set for change, as we described above, is imminently doable. Moreover, as we show below, there are currently \$14 trillion in unhedged U.S. assets held by G10 investors that may be looking for a home if anxiety surrounding U.S. policies continues to increase.

Europe’s competitiveness challenge isn’t just about closing growth gaps; it’s about building institutional architecture to attract and retain global capital.

**Exhibit 89:** U.S. Equities Now Account for Over One Third of Total European Equity Portfolios (Up Almost 3X From Just 13% in 2011)

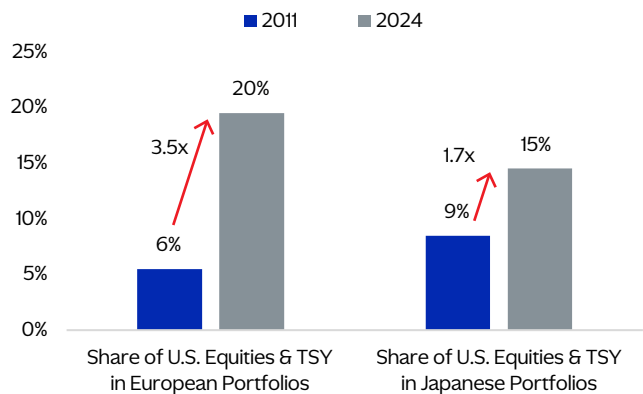
**U.S. Equity Holdings as % of European and Japanese Equity Portfolios**



European ownership refers to domestic holdings of listed shares and ‘rest of world’ equity holdings on a quarterly basis for the U.K., Euro Area and Switzerland to mitigate cross-border measurement errors. Japan ownership refers to Japanese flow of funds data and U.S. Treasury Department data on Japanese-based investors’ holdings (as with Europe, converted to USD based on quarterly avg exchange rates). Data as at December 31, 2024. Source: DB Research, SIFMA, WFE, U.S. Treasury Department, ONS, IMF, ECB, SNB, Federal Reserve.

**Exhibit 90:** Likewise, U.S. Equities and Treasuries Now Account for 20% of European Portfolios (Up From Just 6% in 2011)

**U.S. Equity and Treasury Holdings as % of European and Japanese Portfolios**



European ownership refers to domestic holdings of listed shares and ‘rest of world’ equity holdings on a quarterly basis for the U.K., Euro Area and Switzerland to mitigate cross-border measurement errors. Japan ownership refers to Japanese flow of funds data and U.S. Treasury Department data on Japanese-based investors’ holdings (as with Europe, converted to USD based on quarterly avg exchange rates). Data as at December 31, 2024. Source: DB Research, SIFMA, WFE, U.S. Treasury Department, ONS, IMF, ECB, SNB, Federal Reserve.

**QUESTION NO. 2**

## What is your latest thinking on the retirement market for individual investors?

Like many nations across the globe, the U.S. faces a retirement crisis. Longevity has increased, while average retirement ages have remained broadly unchanged in the mid-60s, leading to an extension of retirement funding needs. We think this is why many regulatory bodies, such as the DOL and SEC, along with the White House, might consider policy changes that could advance access to retirement security. KKR has been a pioneer in the retirement security business since 1976 when we began managing capital on behalf of public and corporate pension funds, as well as insurance companies. These companies and public plans have long recognized the importance of allocating a portion of their investment portfolio to Alternatives, with the beneficiaries of this

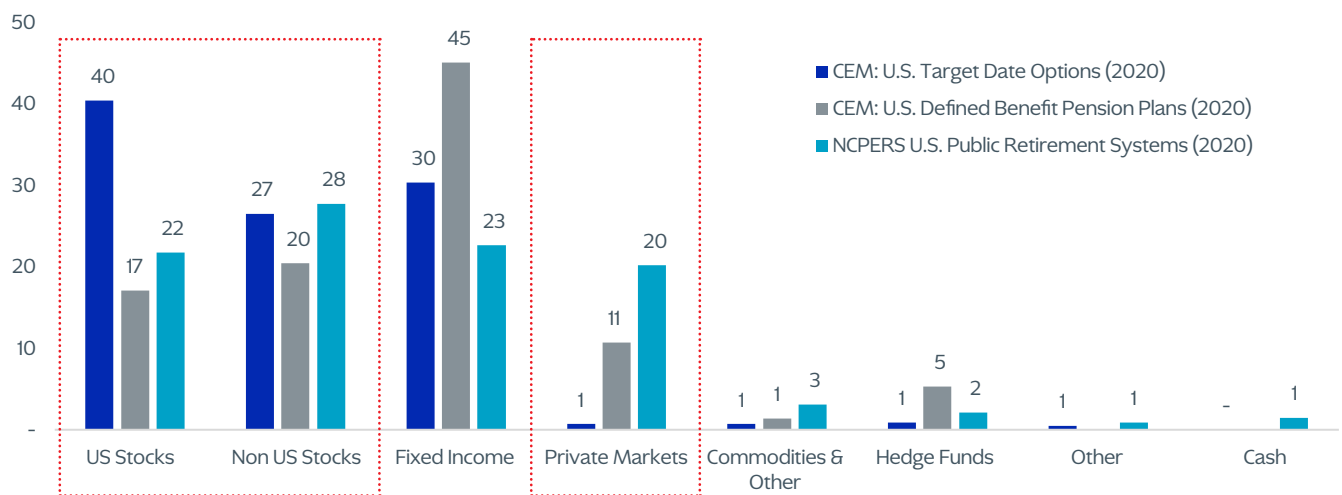
approach including firefighters, teachers, police and many other public and private sector workers. So, it didn't come as a surprise to many of our clients when we extended that mandate in 2021 by acquiring Global Atlantic, a leading provider of annuity and insurance solutions. Today, Global Atlantic serves over 3.5 million policyholders through a broad range of tax-advantaged, income-focused vehicles that are designed to meet the long-duration liabilities of retirement.

What has surprised some, however, is why KKR (and other firms like ours), despite our deep presence in pensions and insurance, has not yet fully brought our investment capabilities to the defined contribution market, particularly the nearly \$10 trillion 401(k) segment. It's a fair question. After all, the 401(k)—first codified in the Revenue Act of 1978—has become the dominant retirement vehicle for corporate employees, growing from a few hundred plans in the early 1980s to well over 700,000 today, with more than 70 million active participants<sup>2</sup>.

<sup>2</sup> Data as at 2024. Source: ICI.

**Exhibit 91: U.S. Target Date Funds Have Higher Allocations to Public Equities and Much Less Exposure to Private Markets, Compared to U.S. Defined Benefit Plans and Particularly to U.S. Public Pension Plans**

### Asset Allocation Comparison, %



Data as at December 31, 2020. Source: U.S. Target Date options and Defined Benefit plans: Average allocation for all target date options in the Cross-border Equity Market (CEM) database where unbroken survey data is available from 2011 to 2020, as shown in the study "Has the lack of asset diversification in DC retirement plans been a costly missed opportunity?" conducted by Georgetown University. Public Retirement Systems; NCPERS 2025 Public Retirement Systems Study: Trends in Fiscal, Operational, and Business Practices.



Consider just how different many 401(k) plans' asset allocation approaches are relative to defined benefit and insurance products, despite largely serving the same types of long-term focused future retirees. Indeed, just consider the gap in allocation between traditional pensions, which often hold 25-35% of their portfolios in Alternatives, and annuity writers, which typically have 5-10% of their assets directly in Alternatives (and upwards of 31% in non-traditional assets; see our latest [Insurance Survey No Turning Back](#)) versus 401(k) plans, which essentially hold close to none of their assets in non-traditional investments. One can see this in *Exhibit 91*, which shows the typical 401(k) participant in a Target Date Fund (TDF) has nearly zero allocation to Private Equity, Private Credit, Real Estate, and Infrastructure. At the same time, the average corporate pension is about 22% in Private Markets and Hedge Funds.

This has real consequences. As our colleague Rachel Li has noted in our work on capital market assumptions and retirement savings, asset allocation is the primary driver of long-term outcomes, particularly in the retirement space. Asset allocation matters even more than fees or manager selection, although those are obviously important as well. If you are a long-term investor, the absence of higher returning, less correlated assets in your portfolio could be a missed opportunity and almost certainly a structural disadvantage.

Georgetown University's Center for Retirement Initiatives has now put hard numbers around something we have long suspected: a modest allocation to Private Equity and Real Assets can materially upgrade professionally managed Target Date Funds without ratcheting up risk. In back testing three scenarios that substitute just 10 percent of a standard glide-path, the researchers found that a split sleeve (5% PE/5% Real Assets replacing a mix of U.S. large-cap equities and core bonds) delivered the best diversification profile, with 82% of periods outperforming and a 15 basis points annualized median uplift.<sup>3</sup>

The study suggested that by scaling those 15 basis points across every U.S. TDF, the incremental return approached \$5 billion a year, roughly \$35 billion if applied to the entire defined-contribution market. For an individual saver, that

gain translates into about \$2,400 of extra spending power each year in retirement.<sup>4</sup> Georgetown's analysis suggested that DC plans have already narrowed the performance gap with DB peers—from 180 basis points a year (1998-2005) to 46 basis points (2007-2016)—largely because the assets have migrated into professionally managed TDFs. Georgetown's work also suggests the next leg of that catch-up will come from embracing the illiquidity premium that DB plans have utilized for decades.

Our thesis is playing out in other metrics that we follow too, including age of participant. All told, as of year-end 2022, more than 40% of 401(k) participants were in their 20s or 30s, and another 23% were in their 40s. Nearly half had five years or less of tenure, including almost a quarter who were recent hires. These demographics matter not just for contribution patterns but for how capital is allocated across time and the potential for compounding.

While we are still gathering more comprehensive data, the average hold period or asset turnover across platforms is revealing: pension funds tend to be multi-decade investors; annuity portfolios hold assets on an average 7-12 year horizon; in contrast, 401(k) funds, while often held for decades, are often optimized for daily liquidity and quarterly statements, not duration-matched income, for a retirement potentially lasting 25 to 30 years. These frictions—liquidity requirements, daily valuation standards, fee disclosure rules—are real, but they are increasingly solvable.

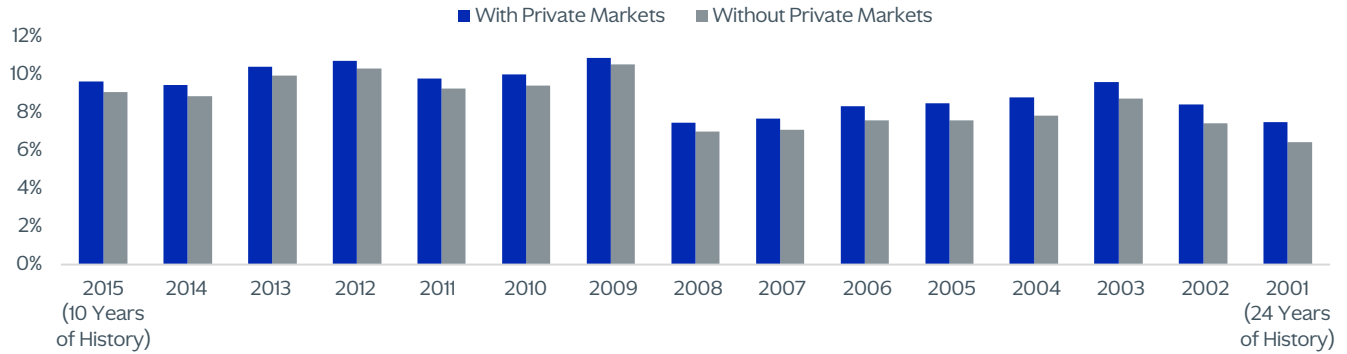
This system has benefits, such as simplicity, automation, and market participation, but also limitations. The lack of diversification into Private Markets, inflation-sensitive assets, and uncorrelated return streams, especially for employees closer to retirement, means most DC participants are exposed to a narrow slice of the global capital stack. In a world of *Regime Change* and compressed forward returns, the 401(k) may face some structural challenges that were not as prevalent when it was conceived. It is not surprising, then, that policymakers are considering regulatory clarification for allocators to defined contribution plans to act in similar ways as those who allocate defined benefit and insurance plans.

3 Georgetown University Center for Retirement Initiatives, "Greater Asset Diversification Can Materially Improve Outcomes," June 2023.

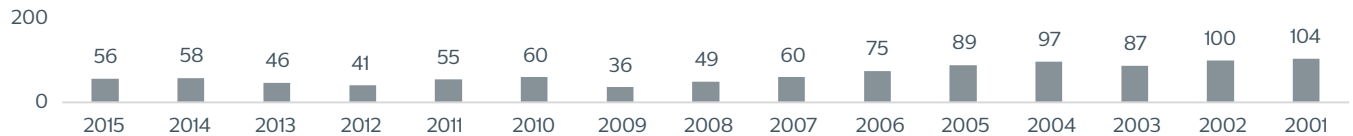
4 Georgetown's analysis was based upon a 40-year savings horizon and 20-year draw-down of professionally managed Target Date Funds.

**Exhibit 92: On an Annualized Basis, the Addition of Alternatives Could Enhance Net Return by Approximately 70 Basis Points per Year, Based on Historical Data**

**Annualized Net Returns for 25-Year-Old Investors Starting in Different Years, Assuming a Typical Target Date Fund Glide Path**



**Annualized Net Return Uplift/(Drag) With 20% Private Markets, Basis Points**



For Illustration Purposes Only. The private market portfolio is composed of 60% Private Equity, 15% Private Credit, 15% Real Estate, and 10% Infrastructure, reflecting an approximate historical market-cap-weighted allocation across Private Markets as per Burgiss. Realized annualized compounded net of fees returns and realized annual calendar year volatilities are calculated using the following proxies from 2000 to 2024: Global Buyout: Cambridge Buyout Index; Private Infrastructure: Burgiss Infrastructure Index/Generalist, Value-Add, Opportunistic; Private Real Estate: Burgiss Real Estate Index/Value-Add, Opportunistic; Private Debt: Burgiss Private Debt Index. Data as at June 30, 2025. Source: Bloomberg, Cambridge, Burgiss, S&P, MSCI, KKR Global Macro & Asset Allocation analysis.

Why are we believers in the performance benefits of adding Alternatives to Target Date Funds? We note the following:

**Point #1: Target Date Funds are chronically under-diversified.**

- The typical U.S. target-date option keeps approximately 67% in Public Equities and very little in Private Markets, whereas defined-benefit and public-pension peers hold materially more in Private Equity, Private Credit, Real Estate, and Infrastructure. This high concentration in Public Equities leaves TDF investors over-exposed to equity beta and under-exposed to contractual, inflation-linked cash-flow streams. Rachel’s work above shows that even a modest sleeve of Private Markets can meaningfully improve the glide path.
- Further, our analysis assumes the typical TDF glide path with a 20% allocation to Alternatives prior to age 50. Within the 20% allocation, the Private Markets portfolio is composed of 60% Private Equity, 15% Private Credit,

15% Real Estate, and 10% Infrastructure, reflecting an approximate market-cap-weighted allocation based on Burgiss data. Using 2000-2024 net returns, which are representative of markets’ average performance without accounting for excess returns from manager selection, the 20% Private Markets allocation adds an average of 70 basis points of annualized net return with lower realized year-over-year volatility. Specifically, for every dollar invested in this hypothetical Private Market-enhanced TDF, it would have generated approximately 30% additional lifetime savings for a participant who started in 2001 and remained invested over 24 years, compared to a traditional TDF. For those who started later in 2015, the 10-year allocation to Private Markets would have created an additional 5% in savings as of 2024.

**Point #2: Risk-adjusted results could be stronger for portfolios that include Private Markets.**

- As Exhibit 94 shows, Private Markets allocations are less correlated with Public Equities and bond

markets, dampening drawdowns and smoothing the wealth path, which we think are critical in the latter stages of the TDF glide path. Our work also suggests that historically, the Sharpe ratio of an Alternatives enhanced portfolio is higher than the plain-vanilla TDF at every vintage.

**Point #3: Structural headwinds identified by our *Regime Change* thesis support the inclusion of Alternatives in investor portfolios.**

- Private Markets capture the illiquidity premium that typical daily-priced TDFs cannot.
- Real Assets such as Real Estate and Infrastructure embed inflation protection and can benefit from the ‘Security of Everything’ capex cycle. Infra, in particular, is a beneficiary of Private Markets stepping in to fill the gaps in government-related expenditures.
- Private Credit and PE give access to idiosyncratic alpha and operational value-creation that passive Public Equities holdings miss.

Bottom line: Our work shows that a 20% allocation to Private Markets can improve long-term retirement outcomes relative to a traditional Public Equities/Bond-oriented glide path—raising compounded returns without an equivalent increase in volatility. In our view, this potential reality could serve as an important catalyst for revamping target-date design and democratizing access to the benefits of Alternatives. We have seen this approach work in the context of defined benefit and insurance savings programs, and as such, we believe it would also work as an option for those who offer DC plans.

**QUESTION NO. 3**

## How are you thinking about Relative Value in Credit?

Amidst market volatility stemming from the ‘Liberation Day’ shock on April 2, high-yield spreads widened 150–200 basis points from year-end 2024 to their peak that month. Since then, however, spreads have retraced over 100 basis points, returning close to historical tights. This pattern holds across most credit strategies, where spreads remain compressed, making relative value opportunities within

Liquid Credit increasingly scarce. In contrast, Private Credit still presents pockets of relative value opportunities across private strategies. We assess relative value through two measures of risk: volatility and look-through leverage.

- While spreads across Liquid Credit remain tight, we see attractive opportunities on the margin for shorter duration CLO liabilities due to their spread pick-up against similarly rated loans and bonds and their strong structural protection. CLO BB tranches, in particular, stand out, offering a 300–400 basis point spread pick-up over U.S. HY with comparable post-COVID volatility while benefiting from lower historical default rates due to the structural protections built into CLOs. CLO BB typically comes with an approximate 8% credit enhancement, which means the deals can tolerate close to 22% collateral loss at a 50% recovery rate before getting impaired. Over the long run, this protection translated to a default rate under 1% for CLO BB. That said, one potential risk we are tracking is that the NAIC is considering tougher risk-based capital (RBC) charges for CLO tranches rated BBB and below, a shift that could dampen insurance demand. We also note that the non-IG segment of CLOs only comprises about 5% of the total U.S. CLO universe, making strong security selection essential to mitigate the downside risks.
- Much like CLO liabilities in Liquid Credit, collateral-backed investments in Private Credit, such as Asset-Based Finance and parts of Asia Credit, are increasingly attractive on a risk-adjusted basis. The combination of higher inflation boosting demand for hard assets, and the outbreak of volatility in the banking system prompting banks and corporations to deleverage their balance sheets, boosting demand for financial assets has created a favorable environment for alternative lenders and investors. As the asset class matures and expands, it continues to offer meaningful absolute total return potential as well as some notable diversification benefits, particularly for portfolios that remain under-allocated to this segment of Private Credit.
- As a more comparable risk measure across both Liquid and Private Credit, we also analyze the leverage-adjusted returns, which strips out the noise from mark-to-market versus model volatility. Higher corporate leverage generally implies additional risks,

such as earnings volatility. From this perspective, EU credit stands out against U.S. credit, as EU issuers typically operate with lower leverage yet offer higher spreads than their U.S. peers to compensate for the added complexity and fragmentation of the European market. Another compelling asset class, as previously discussed, CLO BB tranches also screen attractively on a collateral-pool look-through leverage basis.

Our bottom line is that recent market volatility reminded us that headline risk can still jolt liquid spreads, but the subsequent snap-back proves an even more important point that traditional high-yield and loan markets remain starved of net supply, and the relative value inside public indices is now razor thin. With HY spreads already clawing back more than 100 basis points, investors hunting for incremental carry must either move down in quality—hardly attractive this late in the cycle—or shift the opportunity set.

Our prescription is clear:

- Consider shifting public credit exposures towards CLO BB tranches. At today's levels, they offer 300-400 basis points of spread pick-up versus U.S. High Yield, comparable volatility since 2020, and a structural cushion that historically limits defaults to less than 1 percent. If NAIC risk-charges do rise, we suggest you use that dislocation to add, not exit—but on a name-by-name basis, given the thin 5% share of non-IG paper in the asset class.
- We also suggest rotating incremental dollars into collateral-backed Private Credit. Asset-Based Finance now benefits from two secular tailwinds: Inflation lifts replacement value for hard assets, and bank de-risking creates a durable funding gap. We think that portfolios still underweight ABF have an uncommon chance of locking in equity-like return targets with credit-like downside.
- Don't disregard Europe's leverage discount. Euro-area issuers run lower balance-sheet leverage but pay wider spreads than their U.S. peers—compensating investors for nothing more than market complexity. That is mispriced diversification in a single trade.

In short, we view Credit as a competitive asset class in the *Regime Change* we are envisioning. However, given the lack of new net issuance, investors should stop reaching

for yield in crowded spaces where capital structures could be shaky. Rather, we believe now is the time to climb the capital stack away from unsecured beta towards secured cash-flows that pay you for accepting complexity, not leverage. Embrace the benefit that relative value analysis can deliver and make that rotation before 'the Street' does. If you follow this approach, an investor will truly have made their own luck in the back half of 2025.

#### ● QUESTION NO. 4

## What is your outlook for expected returns?

As we have been highlighting for some time now, our key takeaway remains that investors are still facing a 'flatter' set of expected returns, underscoring our view that the performance differences between various assets are narrowing in the new investing regime we envision. At the same time, investors are experiencing lower returns while historical correlations among assets are changing, making asset allocation a more crucial factor for overall portfolio volatility than the volatility of individual assets. We continue to have high conviction in this framework, and we think that there are several key action items for portfolio managers and CIOs to consider. They are as follows:

1. **A flatter efficient frontier:** The return differential between the best and worst performing assets in a portfolio remains less stark than in the previous five years. Drivers of this view include higher interest rates compared to pre-pandemic levels, rich valuations in U.S. Equities, and less central bank intervention, which tends to benefit longer-duration assets like Equities. More recently, elevated geopolitical uncertainty has contributed to significant volatility in the equity markets. Meanwhile, credit spreads have widened modestly in High Yield, while our long-term view on loss rates has improved at the margin. Consider that our expected five-year forward returns for U.S. High Yield credit are now only 30 basis points below the S&P 500.
2. **Fixed Income as an asset class has become more competitive in our *Regime Change* environment:** We continue to see attractive relative value within Credit, and some of the underlying drivers of this view have

actually improved at the margin. For starters, we continue to expect higher coupons going forward, as we think government bond yields settle near 4% long-term and credit spreads have widened modestly. At the same time, loss rates in High Yield remain very low and have actually fallen slightly, which we think is reflective of the improving quality of the index. Finally, we think the strong technical bid for the absolute yield offered in credit remains intact given how High Yield and Leveraged Loan issuance has slowed dramatically. Overall, we think that multi-asset class Credit accounts that can identify relative value across Public and/or Private Markets are likely tomorrow's winners as demographic forces accelerate the global hunt for recurring income.

3. **We expect more performance from Japanese and European Public Equities than in the past:** We think the backdrop for European/Japanese equities is quite different than it is in the U.S. For starters, Europe is currently undergoing major fiscal expansion, and the monetary backdrop is much more accommodative. We think this backdrop is supportive of some modest multiple re-rating in European Equities. We also think that the central bank not suppressing long-term interest rates via QE is very favorable for the European Financial Services sector (Banks and Insurance), which accounts for nearly 16% of the Euro Stoxx index. Increased defense spending too should help. Against this backdrop, we think investors can expect high single-digit returns on a local currency basis in European Equities. Meanwhile, in Japan, we also think that Equities can generate healthy earnings growth alongside some modest multiple expansion as the corporate sector is undergoing governance reforms. In addition, we think the yen can continue to be appreciated modestly over the next five years, which further boosts expected returns on USD-basis.
4. **We no longer expect U.S. small caps to outperform:** We now expect U.S. small caps, proxied by the S&P 600, to modestly underperform large caps over the next five years. This downgrade largely reflects the structural deterioration of the U.S. small-cap indices, which is evident across a range of metrics including an increasing number of unprofitable companies, lower earnings growth, and lower return on equity. In our view, part of the explanation here is that the best small-cap compa-

nies are increasingly opting for private ownership, which is a trend that we expect to persist. So, while small caps do have more attractive valuations, we think the challenging fundamental backdrop hinders the potential for a meaningful multiple re-rating over the medium term.

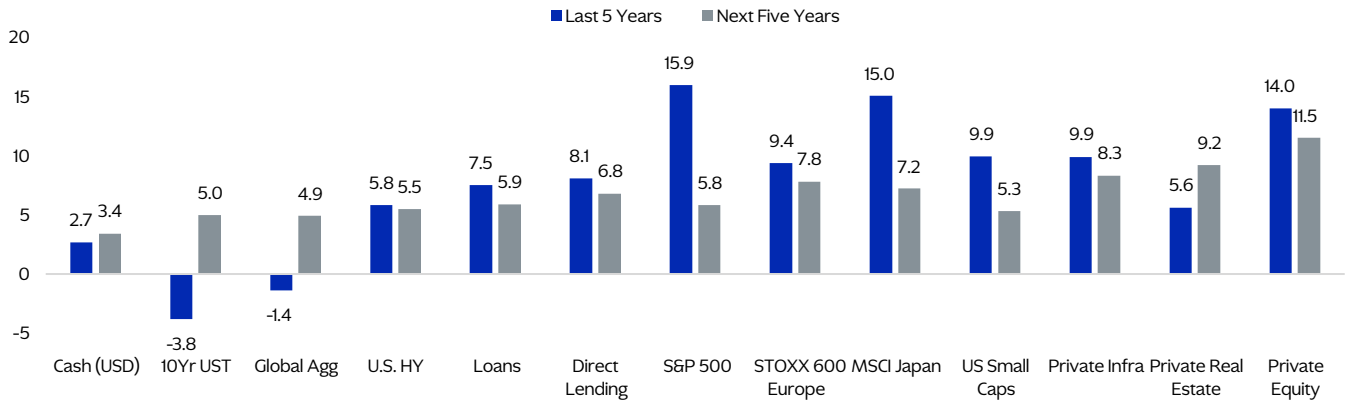
5. **On a go-forward basis, the three horsemen of PE, Real Estate, and Infrastructure remain the best performing Private Markets asset classes.** Across Private Equity, Private Real Estate, and Private Infrastructure, we see not only better structural alignment with the current macro regime, but also higher expected returns relative to historical averages and versus public market equivalents. In our five-year capital markets forecast, all three asset classes screen favorably: Private Equity benefits from dispersion and control, allowing investors to lean into operational improvement and carve-out activity at a time when public multiples are full and growth is harder to find. In Private Real Estate, dislocation has created pricing entry points we haven't seen in over a decade, particularly for assets with cash flow durability and embedded inflation protection. Meanwhile, Private Infrastructure stands out as a structural beneficiary of the global reindustrialization and security of everything themes—capturing policy tailwinds and shifting capital flows. Taken together, these asset classes provide the combination of yield, non-correlation, and inflation-hedging that we believe is essential to navigating what we call *Regime Change*—a world where beta is less rewarding, and alpha must be earned.

Overall, we think that multi-asset class Credit accounts that can identify relative value across Public and/or Private Markets are likely tomorrow's winners as demographic forces accelerate the global hunt for recurring income.



**Exhibit 93: The Three Horsemen of Private Equity, Private Real Estate and Private Infrastructure Should Remain the Top Performance Contributors, We Believe**

**KKR GMAA Expected Returns, %**



For private asset classes (Private Credit, Private Infra, Private Real Estate, and Private Equity) returns are representative of the median manager’s return net of Fee/Carry. Local currency returns shown. Last 5 Year return from May 31, 2020, to May 31, 2025 (2024 for Private Markets) for consistency across asset classes. Data as at June 17, 2025. Source: Bloomberg, BofA, Cambridge Associates, Green Street, KKR Global Macro & Asset Allocation analysis.

**Exhibit 94: Non-Correlation Only Increases in Importance in the Environment We Envision**

**Asset Class Correlations, Quarterly From 2004-2024**

	Public Fixed Income	Public Equities	Asset-Based Finance	Direct Lending	Junior Debt	Private Opportunistic Credit	Real Estate Credit	RE Value-Add & Opp	Buyout	Growth	Venture	Global Infra
Public Fixed Income	-	0.3	0.1	0.0	0.2	0.0	0.4	0.0	0.3	0.2	0.1	0.2
Public Equities	0.3	-	0.5	0.7	0.7	0.7	0.3	0.4	0.8	0.8	0.5	0.6
Asset-Based Finance	0.1	0.5	-	0.7	0.7	0.7	0.2	0.6	0.7	0.5	0.4	0.5
Direct Lending	0.0	0.7	0.7	-	0.8	0.7	0.4	0.5	0.7	0.7	0.5	0.5
Junior Debt	0.2	0.7	0.7	0.8	-	0.8	0.3	0.7	0.9	0.8	0.6	0.8
Private Opportunistic Credit	0.0	0.7	0.7	0.7	0.8	-	0.3	0.6	0.8	0.7	0.4	0.6
Real Estate Credit	0.4	0.3	0.2	0.4	0.3	0.3	-	0.2	0.3	0.4	0.2	0.2
RE Value-Add & Opp	0.0	0.4	0.6	0.5	0.7	0.6	0.2	-	0.7	0.6	0.5	0.7
Buyout	0.3	0.8	0.7	0.7	0.9	0.8	0.3	0.7	-	0.9	0.7	0.8
Growth	0.2	0.8	0.5	0.7	0.8	0.7	0.4	0.6	0.9	-	0.8	0.7
Venture	0.1	0.5	0.4	0.5	0.6	0.4	0.2	0.5	0.7	0.8	-	0.4
Global Infra	0.2	0.6	0.5	0.5	0.8	0.6	0.2	0.7	0.8	0.7	0.4	-

Correlations are calculated with quarterly returns between September 30, 2004 and June 30, 2024. Indices shown for illustrative purposes only to depict the possible diversification benefits of non-traditional asset classes. Each asset class is modeled as follows: Public Fixed Income (Bloomberg Global-Aggregate Total Return Index Value Unhedged USD), Public Equities (MSCI World Index), Asset-Based Finance (KKR Private Credit ABF composite investments post January 1, 2017, Direct Lending (Cliffwater DL Index), Junior Debt (Burgiss Private Debt/Mezz), Private Opportunistic Credit (Burgiss Private Debt/Generalist), RE Credit (Gilberto-Levy Level I Index), RE Value-Add & Opp (Burgiss RE Index: Value-Add/Opportunistic), Global Infrastructure (Burgiss Infra Index), Buyout (Cambridge Buyout), Growth (Cambridge Growth Equity), Venture (Cambridge VC). Source: Bloomberg, Cambridge, Burgiss, Gilberto-Levy, Cliffwater, KKR Global Macro & Asset Allocation analysis.

Looking at the big picture, we think our expected returns work underscores several important investment insights. For starters, we expect much flatter returns than in the past. Against this backdrop, a flatter return profile across more asset classes suggests that upfront yield and non-correlation become more important attributes. It also means that the ability to generate alpha through operational improvement, especially in Private Equity and Infrastructure, becomes a much bigger differentiator, especially relative to Public Equity index-driven beta.

Our work also emphasizes the importance of upfront yield in a lower return environment, and it also raises the importance of low-correlation assets in an increasingly volatile geopolitical landscape. To this end, Asset-Based Finance, Insurance as an Asset Class, and Infrastructure see some multiple re-rating if they can deliver on their investment promise. Finally, GPs who can keep their loss rates lower are likely to outperform, and as such, the ability to focus on relative value across capital structures and geographies and leverage portfolio construction to minimize impairments are most likely to deliver differentiated results.

Given all the crosscurrents shaping today's macro and market environment, our message is to stay the course. The cycle is not over, many investors are still not fully invested, and there are several mega investment themes that have not yet fully played out.

SECTION V

# Key Conclusions

“Luck is what happens when preparation meets opportunity.” —Seneca the Younger

The first half of 2025 has reminded investors that capital markets can ascend, even when geopolitics unsettle, tariffs cause uncertainty, and macro data send mixed signals. The resilience we are describing is no accident; it is a by-product of a potentially underappreciated global easing cycle that is still gaining traction, a technical backdrop starving of net supply, and a corporate sector whose balance sheets never embraced the leverage of prior cycles. Productivity is also being underappreciated at a time of significant innovation. There are also some higher growth, compelling macro investment themes that have kept growth moving along better than market bears have forecasted. Yet, sentiment has generally remained quite poor and therein lies the opportunity, we believe.

To be sure, our message for the balance of the year is not one of complacency. Rather, it is discipline. Without question, the low-rate, low-volatility beta trade that defined 2015–2021 is finished. As we have detailed here and elsewhere, overall returns will likely be compressed. In this new regime, investors must make their own luck by tilting towards assets that rely on collateral-based cash flows, can adjust to rising input costs, and/or enhance operational improvement. That means control-oriented Private Equity, capital-safe segments of Credit, and Real Assets with long-dated, contractual cash flows that can reprice to higher nominal GDP.

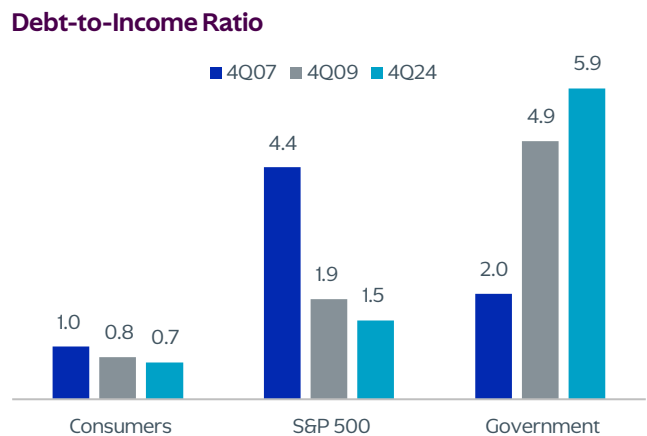
To be sure, our message for the balance of the year is not one of complacency. Rather, it is discipline.

**Exhibit 95:** Trying to Time the Market Can Lead to Missing Out On the Best Days (Remember the Best Periods Typically Follow the Worst Periods)

Price Return by Decade and When Excluding the Decade's Best 10 Days		
Decade	Price Return by Decade	Excluding Best 10 Days per Decade
1930	-42	-79
1940	35	-14
1950	257	167
1960	54	14
1970	17	-20
1980	227	108
1990	316	186
2000	-24	-62
2010	190	95
2020	57	-13
Since 1930	23,555%	67%

Data as at April 7, 2025. Source: BofA Quantitative Research.

**Exhibit 96:** Unlike in the Past, Consumers and Corporations Are Not Overleveraged This Cycle

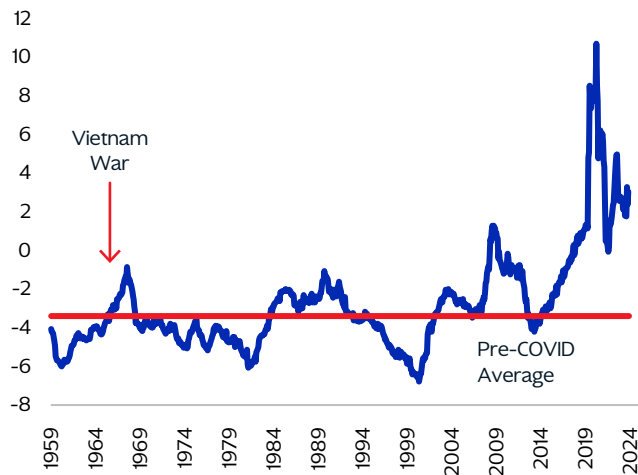


Income is defined as: For consumers total personal income (before tax or interest expense); for corporates it is EBITDA; for government it is total revenue. Data as at December 31, 2024. Source: BofA, KKR Global Macro & Asset Allocation analysis.

At the portfolio level, hedging dollar risk, limiting duration bets and leaning into our durable macro themes—Security of Everything, Productivity/Worker Retraining, Capital Heavy to Capital Light transitions and Collateral-Based Cash Flows remain, in our view, non-negotiable. Yes, stagflation, a heavier U.S. term premium and a weaker currency are real tail risks. However, since COVID, we are of the belief that policy-induced volatility has and will continue to create compelling entry points for long-term investors. In short: keep the glass half full but hold it with two hands—and be ready to act when opportunity, preparation and a little luck converge.

**Exhibit 97:** In Addition to Surging Productivity, Heavy Fiscal Impulses and Low Unemployment Are Key Attributes Defining This Cycle Being Different

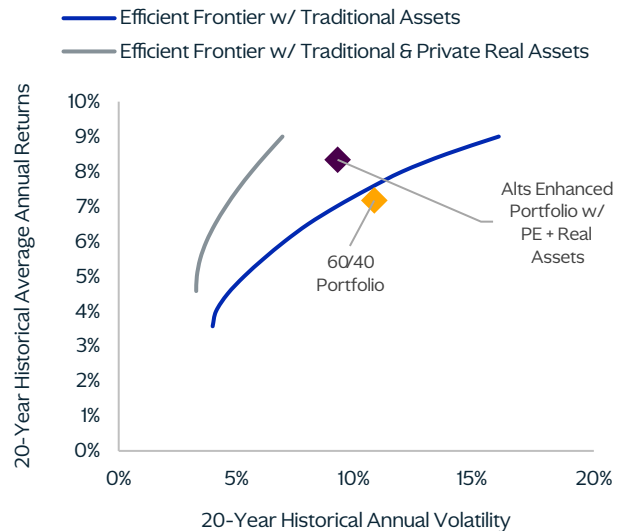
**Difference Between Federal Budget Deficit, as a % of GDP and Unemployment Rate, PPT**



Data as at December 31, 2024. Source: Bloomberg, Haver Analytics, KKR Global Macro & Asset Allocation analysis.

**Exhibit 98:** Our Regime Change Thesis Suggests That Allocators Need to Think Differently About Asset Allocation

**20 Year Average Annual Returns and Volatility of Real Assets and 60/40 Portfolios, %**



Data as at June 30, 2023. Source: KKR Global Macro & Asset Allocation analysis.

At the portfolio level, hedging dollar risk, limiting duration and leaning into our durable macro themes—Security of Everything, Productivity/ Worker Retraining, Capital Heavy to Capital Light transitions and Collateral-Based Cash Flows remain, in our view, non-negotiable.

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