

Weekly commentary

August 4, 2025

BlackRock

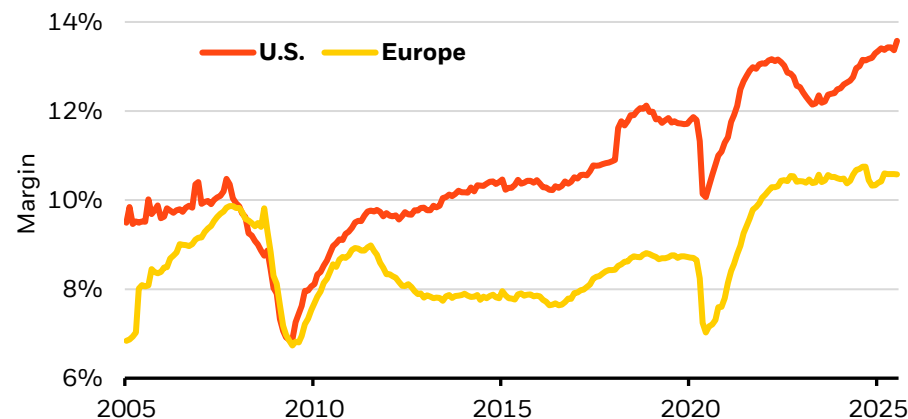
U.S. tug-of-war: earnings vs. tariffs

- U.S. corporate earnings resilience persists as tariff impacts become clearer. We stay overweight U.S. stocks but get granular while assessing the tariff fallout.
- U.S. stocks fell and bond yields slid after soft U.S. jobs data suggested slowing activity. We see many macro crosscurrents at play, muddying the outlook.
- U.S. trade data will show how much tariffs are impacting imports. The Bank of England is expected to cut policy rates.

We see risk assets in a tug-of-war between solid U.S. corporate earnings, powered by the artificial intelligence (AI) theme, and tariffs hurting growth while lifting inflation. Q2 earnings results suggest the AI theme is winning, but questions remain about who will pay for tariffs. Early signs indicate a mix of consumers and companies. We think U.S. corporate strength could cushion the blow and stay overweight the AI theme and U.S. stocks. We get granular when eying the tariff hit.

U.S. corporate strength

U.S. and European corporate profit margins, 2005-2025



Forward-looking estimates may not come to pass. Index performance does not reflect fees. Indices are unmanaged and one cannot invest directly in an index. Source: BlackRock Investment Institute, with data from LSEG Datastream, July 2025. Note: The lines show the 12-month forward profit margins for U.S. and Europe equities. The indexes are the MSCI USA and the MSCI Europe.

The U.S. “reciprocal” tariffs announced on April 2, which stoked historic market volatility, are now taking shape as the U.S. reaches agreements or imposes higher levies. U.S. tariffs on imports are now ending up at an effective rate around 15-20%, higher than we expected earlier this year, and generated revenues of \$27 billion in June, Treasury data show. That means someone is paying the tariffs – and how much they hurt growth and stoke inflation will depend on who pays. Ultimately it is some mix of foreign suppliers, U.S. companies via profit margins and consumers via inflation. Yet U.S. corporate earnings are robust: Q2 U.S. earnings are up about 8% year-over-year even with tariffs, LSEG data show. U.S. profit margins are at record highs relative to flat margins in Europe. See the chart. U.S. mega cap tech is lifting AI investment as seen with Microsoft and Meta last week.



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The slew of trade agreements announced in recent weeks removes some of the uncertainty of the ultimate effective landing zone for tariffs – even if they’re several times higher than where they were at the end of 2024. The tariff impact on U.S. consumers has been slow to show up in part because companies rushed to import goods before expected tariffs in April. Tariffs do not apply to ships that left the port, shipping can take several weeks and companies can delay payments even when goods arrive. Many have not yet raised prices until they have greater clarity. Yet that offset is fading: second quarter U.S. inflation data showed durable goods prices rising at the fastest pace since 1991 outside the pandemic. So consumers are starting to pay some of the tariff costs, especially in household appliances and electronics. And companies have also started paying: global automakers, some of the most exposed to tariffs, are reporting large earnings writedowns.

Automakers highlight how complicated the tariff story is. U.S. automakers like General Motors and Ford are among those taking the large profit hits as tariffs are implemented – and chose to eat the tariffs. Japanese and South Korean automakers are absorbing tariff costs by cutting the prices of the vehicles they sell to the U.S. This pressure on pricing is especially acute in Europe where automakers battle with China’s cheaper electric vehicles and are constrained in raising prices. By contrast, quality producers like Ferrari are lifting prices – highlighting the importance of pricing power.

This is why corporate earnings resilience matters, in our view. Automakers are manufacturers. The industrials sector – where supply chains are among the most integrated globally – is dominated by manufacturers and is likely feeling the biggest impact of tariffs. And yet the industrials sector is the best-performing S&P 500 sector this year, up some 15% compared with 6% for the index, according to LSEG data. Why? Industrials benefit from the AI buildout and other key themes driven by mega forces, such as geopolitical fragmentation and the boost to defense spending this year. That’s why this environment favors getting granular with views below the sector level and favors an active approach to achieving returns.

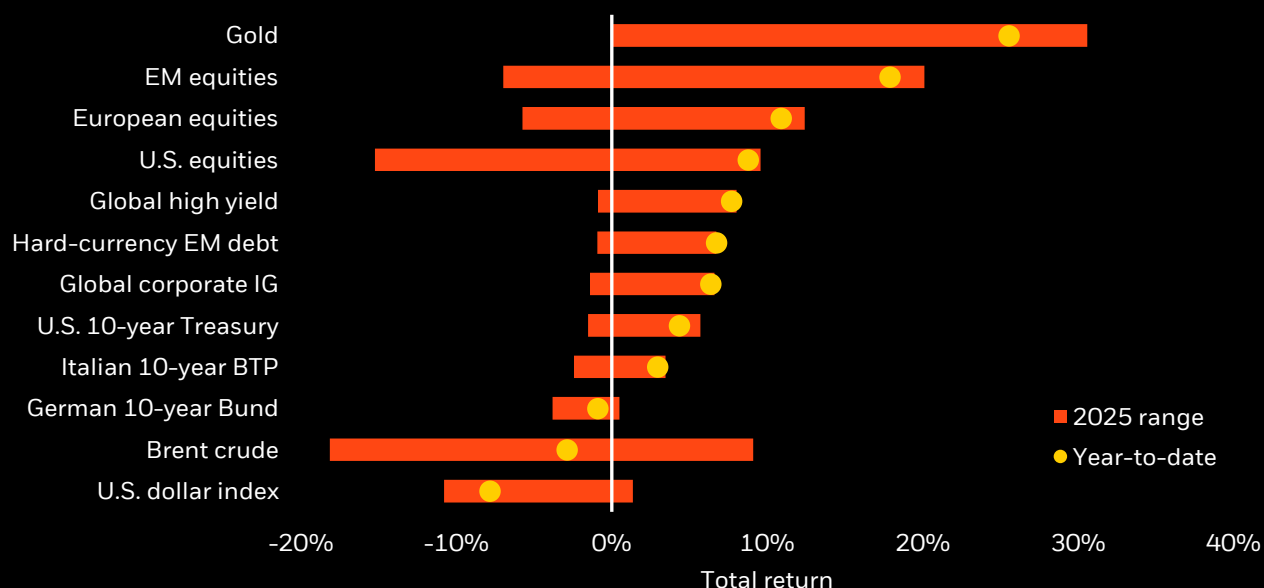
Bottom line: We see a tug-of-war between the economic drag of tariffs and U.S. corporate earnings strength driven by AI. The latter is winning so far, in our view, but getting granular views is key as companies and consumers each eat tariff costs.

Market backdrop

U.S. stocks retreated for the week after pushing to new all-time highs, with the S&P 500 down about 2% for the week. Surprisingly weak payrolls data put stocks under pressure and pushed down Treasury yields on expectations for Federal Reserve rate cuts. We think the payrolls data shows activity slowing but that there are several crosscurrents at play when it comes to inflation (sticky wage growth, tariffs) and for risk assets (the AI theme holding up even as activity has slowed).

Assets in review

Selected asset performance, year-to-date return and range



Past performance is not a reliable indicator of current or future results. Indexes are unmanaged and do not account for fees. It is not possible to invest directly in an index.

Sources: BlackRock Investment Institute, with data from LSEG Datastream as of July 31, 2025. Notes: The two ends of the bars show the lowest and highest returns at any point year to date, and the dots represent current year-to-date returns. Emerging market (EM), high yield and global corporate investment grade (IG) returns are denominated in U.S. dollars, and the rest in local currencies. Indexes or prices used are: spot Brent crude, ICE U.S. Dollar Index (DXY), spot gold, MSCI Emerging Markets Index, MSCI Europe Index, LSEG Datastream 10-year benchmark government bond index (U.S., Germany and Italy), Bloomberg Global High Yield Index, J.P. Morgan EMBI Index, Bloomberg Global Corporate Index and MSCI USA Index.

Week ahead

Aug. 4	China Caixin services PMI	Aug. 7	Bank of England policy decision
Aug. 5	U.S. trade data	Aug. 8	China July CPI

The Bank of England (BoE) is expected to cut interest rates by a quarter-point this week. We think sluggish economic growth and some signs of softening inflation pave the way for a rate cut. Yet persistent inflation pressures will keep interest rates higher for longer and limit how far the BoE can cut rates. U.S. trade data for July will show how much tariffs are slowing imports, with early data showing a sharp drop during the month.

Big calls

Our highest conviction views on six- to 12-month (tactical) and over five-year (strategic) horizons, August 2025

Tactical	Reasons
U.S. equities	Policy uncertainty and supply disruptions are weighing on near-term growth, raising the risk of a contraction. Yet we think U.S. equities will regain global leadership as the AI theme keeps providing near-term earnings support and could drive productivity in the long term.
Using FX to enhance income	FX hedging is now a source of income, especially when hedging euro area bonds back into U.S. dollars. For example, 10-year government bonds in France or Spain offer more income when currency hedged than U.S. investment grade credit, with yields above 5%.
Seeking alpha sources	We identify sources of risk taking to be more deliberate in earning alpha. These include the potential impact of regulatory changes on corporate earnings, spotting crowded positions where markets could snap back and opportunities to provide liquidity during periods of stress.
Strategic	Reasons
Infrastructure equity and private credit	We see opportunities in infrastructure equity due to attractive relative valuations and mega forces. We think private credit will earn lending share as banks retreat – and at attractive returns.
Fixed income granularity	We prefer short-term inflation-linked bonds over nominal developed market (DM) government bonds, as U.S. tariffs could push up inflation. Within DM government bonds, we favor UK gilts over other regions.
Equity granularity	We favor emerging over developed markets yet get selective in both. Emerging markets (EM) at the cross current of mega forces – like India – offer opportunities. In DM, we like Japan as the return of inflation and corporate reforms brighten the outlook.

Note: Views are from a U.S. dollar perspective, August 2025. This material represents an assessment of the market environment at a specific time and is not intended to be a forecast of future events or a guarantee of future results. This information should not be relied upon by the reader as research or investment advice regarding any particular funds, strategy or security.

Tracking five mega forces

Mega forces are big, structural changes that affect investing now – and far in the future. As key drivers of the new regime of greater macroeconomic and market volatility, they change the long-term growth and inflation outlook and are poised to create big shifts in profitability across economies and sectors. This creates major opportunities – and risks – for investors. See our [web hub](#) for our research and related content on each mega force.

- Demographic divergence:** The world is split between aging advanced economies and younger emerging markets – with different implications.
- Digital disruption and artificial intelligence (AI):** Technologies are transforming how we live and work.
- Geopolitical fragmentation and economic competition:** Globalization is being rewired as the world splits into competing blocs.
- Future of finance:** A fast-evolving financial architecture is changing how households and companies use cash, borrow, transact and seek returns.
- Transition to a low-carbon economy:** The transition is set to spur a massive capital reallocation as energy systems are rewired.

Granular views

Six- to 12-month tactical views on selected assets vs. broad global asset classes by level of conviction, August 2025

We have lengthened our tactical investment horizon back to six to 12 months. The table below reflects this and, importantly, leaves aside the opportunity for alpha, or the potential to generate above-benchmark returns – especially at a time of heightened volatility.

		Underweight	Neutral	Overweight	Previous view	
					●	Previous view
Asset	View	Commentary				
Equities	Developed markets					
	United States				+1	We are overweight. Policy-driven volatility and supply-side constraints are pressuring growth, but we see AI supporting corporate earnings. U.S. valuations are backed by stronger earnings and profitability relative to other developed markets.
	Europe				Neutral	We are neutral. Greater unity and a pro-growth agenda across Europe could boost activity, yet we are watching how the bloc tackles its structural challenges before turning more optimistic. We note opportunities in financials and industries tied to defense and infrastructure spending.
	UK				Neutral	We are neutral. Political stability could improve investor sentiment. Yet an increase in the corporate tax burden could hurt profit margins near term.
	Japan				+1	We are overweight given the return of inflation and shareholder-friendly corporate reforms. We prefer unhedged exposures as the yen has tended to strengthen during bouts of market stress.
	Emerging markets				Neutral	We are neutral. Valuations and domestic policy are supportive. Yet geopolitical tensions and concerns about global growth keep us sidelined for now.
	China				Neutral	We are neutral. Trade policy uncertainty keeps us cautious, and policy stimulus is still limited. We still see structural challenges to China's growth, including an aging population.
	Short U.S. Treasuries				+1	We are overweight. We view short-term Treasuries as akin to cash in our tactical views. We would still lean against the market pricing of multiple Fed rate cuts over the next year.
	Long U.S. Treasuries				-2	We are underweight. Persistent budget deficits and inflation pressures could drive term premium up over the long term, but we see scope for lower yields near term. We prefer intermediate maturities.
	Global inflation-linked bonds				Neutral	We are neutral. We see higher medium-term inflation, but cooling inflation and growth may matter more near term.
Fixed Income	Euro area govt bonds				Neutral	We are neutral. Yields are attractive, and term premium has risen closer to our expectations relative to U.S. Treasuries. We prefer peripheral bonds such as in Italy and Spain.
	UK gilts				Neutral	We are neutral. Gilt yields are off their highs, but the risk of higher U.S. yields having a knock-on impact and reducing the UK's fiscal space has risen. We are monitoring the UK fiscal situation.
	Japanese govt bonds				-1	We are underweight. We see room for yields to rise further on Bank of Japan rate hikes and a higher global term premium.
	China govt bonds				Neutral	We are neutral. Bonds are supported by looser policy. Yet we find yields more attractive in short-term DM paper.
	U.S. agency MBS				+1	We are overweight. We find income in agency MBS compelling and prefer them to U.S. Treasuries for high-quality fixed income exposure.
	Short-term IG credit				+1	We are overweight. Short-term bonds better compensate for interest rate risk.
	Long-term IG credit				-1	We are underweight. Spreads are tight, so we prefer taking risk in equities. We favor Europe over the U.S.
	Global high yield				Neutral	We are neutral. Spreads are tight, but corporate fundamentals are solid. The total income makes it more attractive than IG.
	Asia credit				Neutral	We are neutral. We don't find valuations compelling enough to turn more positive.
	Emerging hard currency				-1	We are underweight. Spreads to U.S. Treasuries are near historical averages. Trade uncertainty has eased, but we find local currency EM debt more attractive.
	Emerging local currency				Neutral	We are neutral. Debt levels for many EMs have improved, and currencies have held up against trade uncertainty. We prefer countries with higher real interest rates.

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