WELLS FARGO
Investment Institute

Market Commentary

Weekly perspective on current market sentiment **July 17, 2025**

Scott Wren
Senior Global Market Strategist

Last week's S&P 500 Index: -0.3%

Starting to feel the effects

Key takeaways

- It seems almost a certainty that, in at least the near and intermediate terms, tariffs on a broad swath of U.S. trading partners will be going up, not down.
- For now, consider trimming overvalued sectors and asset classes like Industrials, Consumer Discretionary, and U.S. Small Cap Equities. We expect better buying opportunities later this year.

As the markets were watching the president sign the One Big Beautiful Bill Act (OBBBA) into law, much of the tariff news was put on the back burner as tariffs might still be postponed or negotiated away. Now, with the OBBBA behind us, tariffs are showing they're back as policy priorities. As we enter the early stages of the second-quarter reporting season, investors are going to be laser-focused on how the tariffs have impacted and/or will impact corporate earnings.

It seems almost a certainty that, in at least the near and intermediate terms, tariffs on a broad swath of U.S. trading partners will be going up, not down. The president has set August 1 as the date when some of the most important U.S. trading partners (Mexico, Canada, and the European Union) will see tariffs ranging from 30% to 35% implemented. The U.S. has also sent letters threatening potential tariffs as high as 40% to a number of other countries. The administration has made it a point to repeatedly remind these countries that the U.S. is always open to negotiate trade terms for any that are willing to come to the table and address U.S. concerns of unfair practices and barriers.

So if tariffs are going up, investors are going to need to have some clarity on corporate margins and on price increases to consumers. In other words, if what you sell or the components you purchase to build your product are subject to tariffs, how much of this additional cost is ultimately going to being passed on to the downstream customer? Operating profit margins for the S&P 500 Index have been hovering in the 14% – 15% area (or better) since the third quarter of 2021. That compares to the average operating margin of 12.4% going back to January 1990 according to Bloomberg data.

That means companies do have the ability to absorb some of the cost of any applied tariffs in their margins. During this second-quarter earnings reporting season, investors will want to know first if tariffs will affect the company now or will likely affect it in the future. Secondly, they will want to know how much of that cost is going to be passed on to the buyer and what the magnitude of damage will be to earnings. Those are reasonable questions to be sure.

Our analysis suggests a midsingle-digit earnings growth rate result in the second quarter. That is down from the first quarter and reflects a slightly slower economy but also attempts to take into account tariff headwinds. While many companies are still selling inventory that they "bought ahead" to beat tariff increases, others are starting to see bottom line headwinds.

The Bloomberg consensus shows that two of our favored sectors, Information Technology and Communication Services, are expected to post the best year-over-year earnings results. We look for improved earnings comparisons as we move through the end of this year and into 2026 from Energy (most favorable rated) along with the Utilities and Financials sectors, our other favored sectors.

For now, consider trimming overvalued sectors and asset classes like Industrials, Consumer Discretionary, and U.S. Small Cap Equities where we expect better buying opportunities later this year, likely at the end of the year and into 2026.

Risk considerations

Each asset class has its own risk and return characteristics. The level of risk associated with a particular investment or asset class generally correlates with the level of return the investment or asset class might achieve. **Stock markets**, especially foreign markets, are volatile. Stock values may fluctuate in response to general economic and market conditions, the prospects of individual companies, and industry sectors. **Foreign investing** has additional risks including those associated with currency fluctuation, political and economic instability, and different accounting standards. These risks are heightened in emerging markets. **Small- and mid-cap stocks** are generally more volatile, subject to greater risks and are less liquid than large company stocks.

Sector investing can be more volatile than investments that are broadly diversified over numerous sectors of the economy and will increase a portfolio's vulnerability to any single economic, political, or regulatory development affecting the sector. This can result in greater price volatility. **Communication services** companies are vulnerable to their products and services becoming outdated because of technological advancement and the innovation of competitors. Companies in the communication services sector may also be affected by rapid technology changes; pricing competition, large equipment upgrades, substantial capital requirements and government regulation and approval of products and services. In addition, companies within the industry may invest heavily in research and development which is not guaranteed to lead to successful implementation of the proposed product. The **Energy** sector may be adversely affected by changes in worldwide energy prices, exploration, production spending, government regulation, and changes in exchange rates, depletion of natural resources, and risks that arise from extreme weather conditions. Investing in the **Financial** services companies will subject an investment to adverse economic or regulatory occurrences affecting the sector. Risks associated with the **Technology** sector include increased competition from domestic and international companies, unexpected changes in demand, regulatory actions, technical problems with key products, and the departure of key members of management. Technology and Internet-related stocks, especially smaller, less-seasoned companies, tend to be more volatile than the overall market. **Utilities** are sensitive to changes in interest rates, and the securities within the sector can be volatile and may underperform in a slow economy.

General Disclosures

Global Investment Strategy (GIS) is a division of Wells Fargo Investment Institute, Inc. (WFII). WFII is a registered investment adviser and wholly owned subsidiary of Wells Fargo Bank, N.A., a bank affiliate of Wells Fargo & Company.

The information in this report was prepared by Global Investment Strategy. Opinions represent GIS' opinion as of the date of this report and are for general information purposes only and are not intended to predict or guarantee the future performance of any individual security, market sector or the markets generally. GIS does not undertake to advise you of any change in its opinions or the information contained in this report. Wells Fargo & Company affiliates may issue reports or have opinions that are inconsistent with, and reach different conclusions from, this report.

The information contained herein constitutes general information and is not directed to, designed for, or individually tailored to, any particular investor or potential investor. This report is not intended to be a client-specific suitability or best interest analysis or recommendation, an offer to participate in any investment, or a recommendation to buy, hold or sell securities. Do not use this report as the sole basis for investment decisions. Do not select an asset class or investment product based on performance alone. Consider all relevant information, including your existing portfolio, investment objectives, risk tolerance, liquidity needs and investment time horizon. The material contained herein has been prepared from sources and data we believe to be reliable but we make no guarantee to its accuracy or completeness.

Wells Fargo Advisors is registered with the U.S. Securities and Exchange Commission and the Financial Industry Regulatory Authority, but is not licensed or registered with any financial services regulatory authority outside of the U.S. Non-U.S. residents who maintain U.S.-based financial services account(s) with Wells Fargo Advisors may not be afforded certain protections conferred by legislation and regulations in their country of residence in respect of any investments, investment transactions or communications made with Wells Fargo Advisors.

Wells Fargo Advisors is a trade name used by Wells Fargo Clearing Services, LLC and Wells Fargo Advisors Financial Network, LLC, Members SIPC, separate registered broker-dealers and non-bank affiliates of Wells Fargo & Company. PM-01132027-8174855.1.1