



Jeffrey Schulze, CFA
Managing Director,
Head of Economic
and Market Strategy

The Long View: Push-Pull

Key Takeaways

- ▶ The expected positive forces of the One Big Beautiful Bill Act and future interest rate cuts should soon outweigh the negative forces of tariff actions by the new administration, enabling the economy to reaccelerate into 2026.
- ▶ Investors should look past the noise emanating from a potential second-half slowdown and longer-term normalization in the labor market, bolstered by optimism from a Recession Risk Dashboard that remains solidly expansionary.
- ▶ While stocks have rallied strongly to new highs, history suggests markets have more room to run. Propelled by a growing fiscal impulse, we believe competing policy push-pull forces are improving, meaning any near-term pullbacks should be viewed as buying opportunities for long-term investors.

Trump Policies Creating Tug of War in Markets

In physics, force is an influence that causes an object to speed up, slow down or change direction. It is essentially a push or a pull resulting from the interaction between two objects, as described by Newton's laws of motion. Sometimes forces oppose one another, creating friction or resistance that holds back the movement of an object. This is apt when considering the impacts of the Trump administration's policy agenda, which has generated various opposing forces on economic growth this year. An initial tariff force pushed the S&P 500 Index 18.9% below its February peak in the aftermath of Liberation Day. However, different policy forces expected to positively influence economic and earnings growth in the months ahead helped to pull equities back to new all-time highs by late June.

The first of these positive policy forces is the decline of an unfavorable one, with tariff rates coming down from their announced levels on Liberation Day and trade deals beginning to materialize with the U.K., China and Vietnam. Progress toward the passage of the One Big Beautiful Bill Act (OBBA) has represented a second and larger positive policy force, along with a third in the form of renewed prospects of interest rate cuts from the Federal Reserve.

Taken together, the positive forces should outweigh the negative, although the impact from the OBBA and any rate cuts remain future considerations while the tariff headwinds exist today. As a result, the economy could experience a soft patch in the interim, which may

already be showing up in housing, business investment and consumption data.

We do not believe this soft patch will metastasize into a recession given the coming positive policy forces, primarily from the passage of the OBBB on July 2. Our optimistic outlook is reinforced by the output from the Clearbridge Recession Risk Dashboard, a group of 12 economic and market indicators that have historically foreshadowed a looming recession. There were no indicator changes in June and the overall dashboard reading remains solidly in green expansionary territory.

Exhibit 1: U.S. Recession Risk Indicators

	June 30, 2025	March 31, 2025	December 31, 2024
Consumer	Housing Permits	↑	↑
	Job Sentiment	×	×
	Jobless Claims	↑	↑
	Retail Sales	↑	↑
	Wage Growth	↑	↑
Business Activity	Commodities	↑	↑
	ISM New Orders	×	●
	Profit Margins	↑	↑
	Truck Shipments	●	●
Financial	Credit Spreads	↑	↑
	Money Supply	↑	●
	Yield Curve	×	●
Overall Signal		↑	↑

↑ Expansion ● Caution × Recession

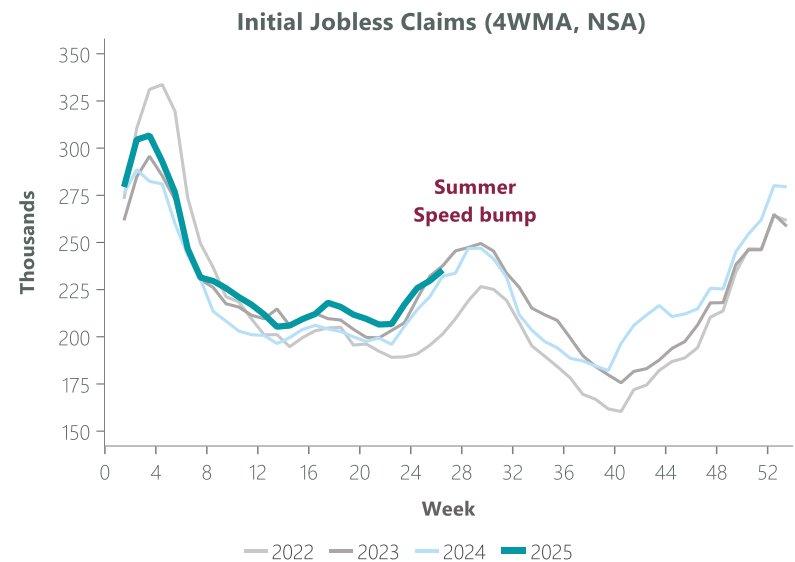
Data as of June 30, 2025. Sources: BLS, Federal Reserve, Census Bureau, ISM, BEA, American Chemistry Council, American Trucking Association, Conference Board, Bloomberg, CME, FactSet and Macrobond. The ClearBridge Recession Risk Dashboard was created in January 2016. References to the signals it would have sent in the years prior to January 2016 are based on how the underlying data was reflected in the component indicators at the time.

One dashboard indicator in particular focus lately has been initial jobless claims, which measures the number of first-time filers for unemployment benefits and thus provides a good reading on how many job losses may be occurring at any point in time. We place extra emphasis on this specific indicator due to its strong track record, high frequency (weekly release), and the fact that it typically sees only minor revisions, meaning the data can be largely taken at face value. However, initial jobless claims have followed an unusual seasonal pattern in recent years, with an early summer pickup followed by a drop as back-to-school hiring occurs.

A New Normal Labor Market

As a result, we are focusing on the non-seasonally adjusted initial claims data relative to the same week from prior years, which provides a better reading than the headline and seasonally adjusted figures in our view. Through this lens, the data looks less concerning, and we believe investors should look past the noise emanating from this typical summer swoon.

Exhibit 2: Dashboard Indicator - Initial Jobless Claims

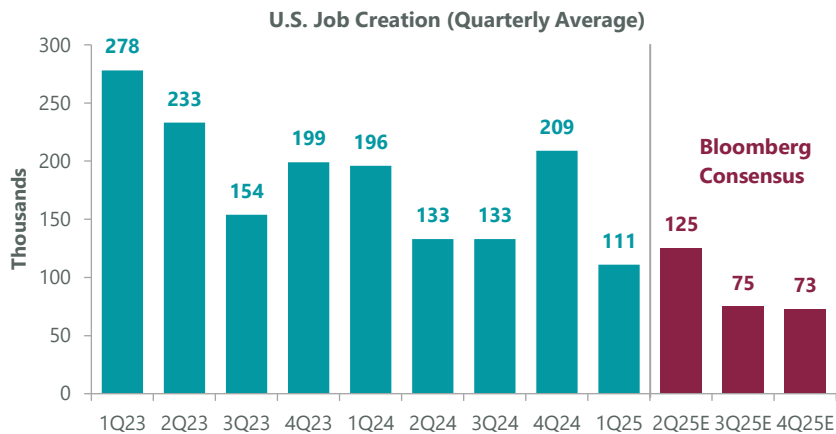


Note: 4WMA stands for four-week moving average, and NSA stands for non-seasonally adjusted. Sources: U.S. Department of Labor, Macrobond. Data as of July 3, 2025.

The health of the labor market is likely to remain a key focal point in coming quarters as investors assess the health of the U.S. economy and the prospect for Fed rate cuts. However, the market may need to recalibrate its view regarding the “normal” level of job growth. The pace of job creation has been slowing since the exit from the pandemic, with a monthly average of 216k in 2023, 168k in 2024 and 130k in the first half of 2025. Looking ahead, consensus expectations are for average monthly job growth of 74k in the second half of the year.

A drop below 100k would have been viewed as a negative as recently as a few months ago, but headwinds from DOGE-related layoffs, an aging population and reduced immigration flow all suggest that job creation below 100k may become the “new normal.” A slowing pace of job gains isn’t atypical as an economic cycle matures, but at the same time it also doesn’t mean that the cycle has ended.

Exhibit 3: Labor Slowdown Ongoing

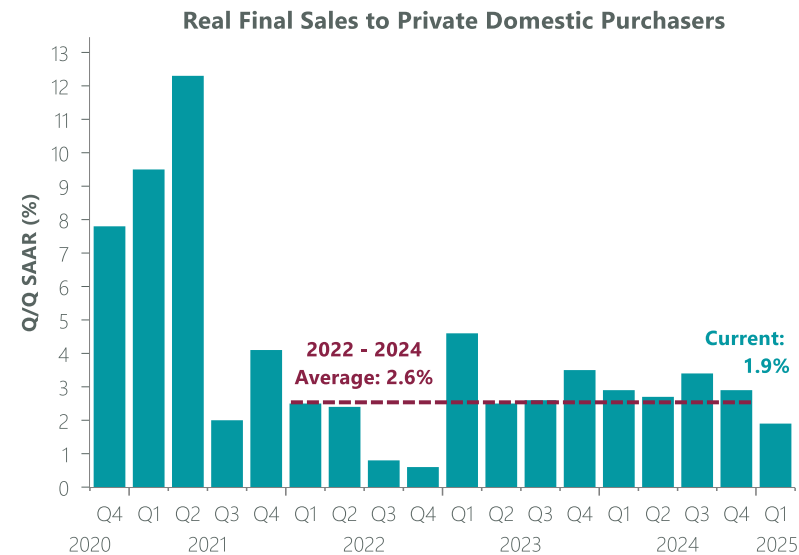


Note: Quarterly average change in non-farm payrolls. As of June 30, 2025. Sources: Bloomberg, U.S. Bureau of Labor Statistics (BLS), Macrobond.

The combination of a soft patch and a maturing cycle could lead to renewed recession fears. This may be amplified by near-term volatility in economic data that is likely to result from the pull-forward and subsequent “air pocket” in demand that have occurred around tariffs. The primary cause of the negative first-quarter GDP reading was a huge surge in imports as companies and individuals rushed to bring goods into the country ahead of Liberation Day. A rise in imports is a negative for GDP, and in the first quarter the contribution was an astounding -4.7% to overall economic growth.

Looking ahead to the second-quarter GDP data that will come out later this month, imports are likely to plummet as businesses and individuals work through the extra stock/inventory they brought in ahead of the increase in tariffs, which should boost measured GDP as the drag from imports declines. Alternative or “core” GDP concepts such as Real Final Sales to Private Domestic Purchasers, which strips out volatile trade (imports and exports) and inventories, along with government spending, which is less relevant to equity markets, are likely to provide a better near-term reading on the underlying health of the U.S. economy. This measure has been running at 2.6% over the past two years and the first-quarter reading was consistent with the lower end of that trend at 1.9%.

Exhibit 4: Core GDP Guides the Way



Q/Q SAAR stands for quarter-over-quarter change, seasonally-adjusted at annual rate. Sources: U.S. Bureau of Economic Analysis (BEA), Macrobond. Data as of June 26, 2025, latest available as of June 30, 2025.

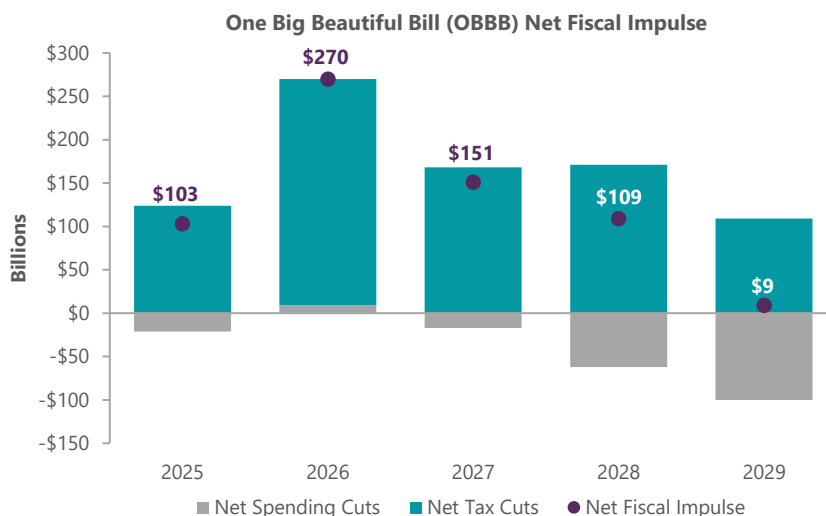
In the coming quarters, tariff distortions should give way to tailwinds from positive policy forces, namely the tax cuts included in the OBBB. The legislation is expected to generate a peak fiscal impulse of approximately 1% of GDP in 2026, on top of the extension of the 2017 Tax Cuts and Jobs Act tax cuts. Individual tax cuts should begin to be felt by early fall as withholding tables are adjusted for no taxes

on overtime or tips, while the bulk of the impact will occur in the first half of 2026 when individuals complete their tax returns.

Companies to Benefit First from Big Beautiful Bill

However, corporate tax filing season actually occurs in the fall (September 15 corporate deadline) and many of the OBBB corporate tax provisions are retroactive to January 1, meaning the corporate tax impacts are likely to begin appearing this quarter. These include expensing for factories and a larger R&D credit, both of which should help spur economic growth.

Exhibit 5: Tax Tailwind



Data as of June 30, 2025. Based on CBO Scoring of Senate One Big Beautiful Bill Act on June 27th.
Source: Wolfe Research.

It is important to note that the OBBB is not cost free — the Congressional Budget Office (CBO) estimated that the initial version proposed by the Senate would add \$3.3 trillion to the deficit over the next 10 years, leading to renewed fears about federal debt sustainability. While the final cost of the bill will be different (it has changed since the CBO scoring occurred, but newer versions were not yet available as of publication), it appears unlikely to be less than the \$2.8 trillion in revenue the CBO estimates tariff changes will bring in over the same period. Although the U.S. deficit is on an unsustainable path, we believe the outlook over a five-year investable horizon is manageable, meaning these concerns are likely to flare up but remain secondary in the coming years.

In the interim, other concerns are more likely to drive market choppiness. For financial markets, the possibility of near-term volatility seems higher than usual as many of the potential positives such as the OBBB impacts appear to be largely “priced in” to equity valuations. Put differently, markets may be ahead of the coming good news and reduction in uncertainty, [a factor that we highlighted last quarter](#) as being a key driver of upside as clarity emerged.

Temporary setbacks that increase uncertainty could cause the market to stumble, even if the longer-term outlook remains healthy.

U.S. equities have proven resilient in the face of a different source of uncertainty over the past few weeks: an increase in geopolitical tensions between Iran and Israel. That pressure has already begun to wane, and history shows that such conflicts tend to be short-lived in terms of their market disruption. Since 1950, the S&P 500 has achieved positive returns of 1.4%, 2.8% and 5.9% in the one, three and six months (respectively) following significant geopolitical events.

Exhibit 6: Buy the Geopolitical Dip?

Geopolitical Event	Date	S&P 500 Price Return (%)		
		1 Month	3 Months	6 Months
Korean War	June 1950	-10.0%	1.5%	4.9%
Vietnam War starts	Nov. 1955	7.3%	4.1%	13.9%
Suez Crisis	Oct. 1956	-4.4%	-3.6%	-1.4%
1958 Lebanon Crisis	July 1958	5.3%	12.1%	23.8%
Cuban Missile Crisis	Oct. 1962	5.4%	13.3%	21.1%
Indo-Pakistani War	Aug. 1965	2.6%	7.7%	8.7%
Six-Day War	June 1967	3.3%	6.5%	7.7%
Arab-Israeli War	Oct. 1973	-4.5%	-10.0%	-15.3%
Fall/Liberation of Saigon	April 1975	4.4%	1.8%	2.3%
Iran Hostage Crisis	Nov. 1979	4.2%	11.6%	3.0%
Soviet-Afghan War	Dec. 1979	5.4%	-8.0%	6.7%
Iran-Iraq War	Sept. 1980	1.2%	4.1%	2.8%
Multinational Force in Lebanon	Aug. 1982	4.9%	13.9%	27.4%
1986 U.S. Bombing of Libya	April 1986	-1.4%	-1.7%	0.5%
U.S. Invasion of Panama	Dec. 1989	-1.1%	-0.4%	4.7%
Gulf War	Aug. 1990	-8.2%	-11.3%	-2.4%
Croatian War	March 1991	1.4%	0.7%	3.7%
Bosnian War	April 1992	2.8%	2.0%	0.4%
Kosovo War	Feb. 1998	4.4%	4.6%	-2.1%
War in Afghanistan	Oct. 2001	4.1%	8.7%	4.8%
Iraq War	March 2003	2.0%	13.7%	18.3%
Russian Invasion of Ukraine	Feb. 2022	2.6%	-10.3%	-2.8%
Average		1.4%	2.8%	5.9%

Data as of June 30, 2025. Sources: FactSet, S&P.

Climbing the latest wall of worry, the S&P 500 recovered to its previous highs in just 55 trading days from the April 8 lows, taking many by surprise and contributing to views that all the good news has already been priced in. While many investors remain on the sidelines waiting for a pullback, history shows the S&P 500 has delivered returns of 6.4%, 10.5% and 16.4% in the three, six and 12 months (respectively) after the previous 10 best 50-day rallies since 1950 (the current rally ranks #10), suggesting further upside in the months to come if history is a guide.

Exhibit 7: Strongest 50-Day Rallies in History

Ten Largest 50-Day Rallies Since 1950				
End of 50-Day Rally	50-Day % Change	S&P 500 Index Return		
		3 Months	6 Months	12 Months
June 3, 2020	39.6%	10.6%	17.4%	34.3%
Oct. 22, 1982	35.5%	3.6%	15.6%	19.5%
May 19, 2009	34.2%	9.7%	20.6%	22.8%
March 6, 1975	26.9%	10.5%	2.4%	18.4%
Dec. 18, 1998	23.8%	10.8%	13.0%	19.6%
Sept. 16, 2009	21.3%	3.8%	8.5%	5.2%
June 24, 1997	20.5%	5.4%	4.1%	26.4%
March 26, 1991	20.4%	-1.3%	2.7%	8.4%
Jan. 7, 1963	19.9%	6.5%	9.5%	18.0%
March 13, 1987	19.7%	4.0%	11.1%	-8.6%
Average		6.4%	10.5%	16.4%
June 20, 2025	19.8%	?	?	?

Note: Distinct 50-Day rallies. Sources: S&P, FactSet.

Although the next several months may see a period of consolidation for U.S. equities, the longer-term outlook looks more favorable. The timing distortions and “air pocket” from tariffs should give way to an improved fiscal impulse that should help power economic reacceleration into 2026. We believe these competing policy push-pull forces are on balance improving for equity investors and could be amplified by Fed rate cuts later in the year. As a result, should volatility emerge in the coming months, we believe long-term investors will be best served by buying into any weakness.

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