DSG
Capital Advisors

2025 Mid-Year Review & Second Half Outlook

In our 2025 Outlook, we posed the question, *"What should investors expect to see unfold in 2025?"* We noted that after the S&P 500 returned more than 25% in 2023 and 2024, it was unlikely to see 25% returns in three consecutive years.

We cited history as our guide. Specifically, we noted that over the past 100 years there have only been 7 instances with 20% returns in 2 consecutive years. Moreover, in only 4 of those 7 instances did the third year provide positive returns: 1944 +19.8%, 1956 +6.6%, 1984 +6.3% and 1997 +33.3%.

Finally, we noted that there has only been **one instance** over the past 100 years when the S&P 500 rose 20+% three or more years in a row. During the period of 1995 – 1999, the S&P 500 posted +20% total returns in **five consecutive years:** 1995 +37.6%, 1996 +23.0%, 1997 +33.3%, 1998 +28.6% and 1999 +21%.

S&P 500 Total Returns by Year Since 1926

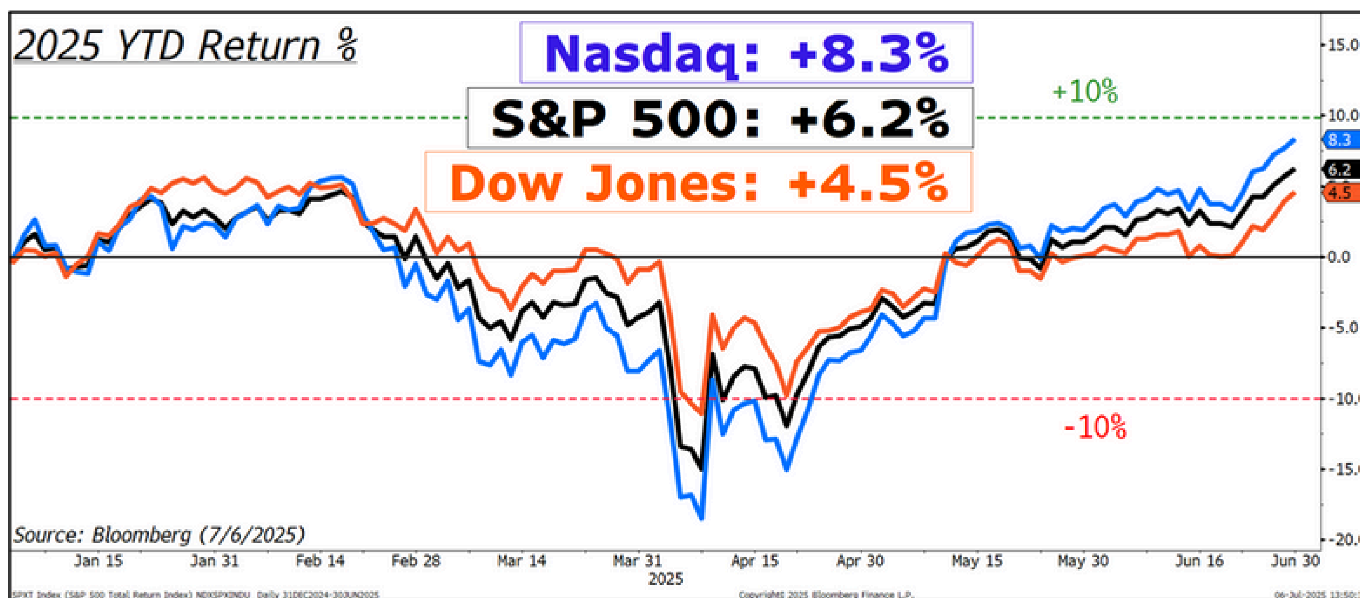
To start this year, we stated that we thought 2025 could be a year of positive returns:

> *At DSG Capital Advisors, we start 2025 with healthy optimism and believe that, absent unforeseen shock to the markets, conditions are positioned so that the S&P 500 could very well provide positive returns in 2025. But with history as our guide, we think the probability of another year of +20% returns in 2025 is unlikely unless several of the key issues discussed below come into perfect alignment.*

To begin the year, we identified six themes that we believed would be the key drivers of market performance in 2025: (1) US debt levels, (2) New Administration policies, (3) Federal Reserve and interest rates, (4) Inflation, (5) AI transitioning from "build out" to "implementation," and (6) Corporate earnings growth.

Now that we are half-way through 2025, our opinion from the start of the year has not changed. However, as more time has passed, we are increasingly confident that 2025 could be more reminiscent of the late 1990s in terms of forward stock returns. In the following pages, we explain why.

US Stock Returns - First Six Months of 2025



In the first six months of 2025, the major US stock indices posted positive single digit returns. If you only looked at the first half returns with the S&P 500 up +6.2%, you might conclude that the start to the year was relatively "quiet." However, nothing could be further from the truth.

As illustrated in the chart above, the Trump Administration's tariff policy caused the S&P 500 to decline almost -20% from its February 19th high. The S&P 500 bottomed April 8th, the day before President Trump announced a 90-day delay in tariffs.

The tariff issue has not been fully resolved yet, with the Administration continuing to announce tariff dealmaking deadlines. Will the stock market face rapid declines again? We don't think so.

Asset Class Returns

Investment Class	Investment Style	1H 2025	2024	2023	2022	2021	2020
Stocks	US Large Cap - S&P 500	6%	25%	26%	-18%	29%	18%
	US Large Cap - Nasdaq	8%	26%	55%	-32%	28%	49%
	US Large Cap - Dow Jones	5%	15%	16%	-7%	21%	10%
	US Mid Cap - S&P 400	0%	14%	16%	-13%	25%	14%
	US Small Cap - S&P 600	-4%	9%	16%	-16%	27%	11%
	US Growth - Russell 1000 Growth	6%	33%	43%	-29%	28%	38%
	US Value - Russell 1000 Value	6%	14%	11%	-8%	25%	3%
	Emerging Markets - MSCI EM	15%	7%	10%	-20%	-3%	18%
	Global Markets - MSCI World ex. US	18%	5%	16%	-16%	8%	11%
Bonds	US Aggregate Bonds	4%	1%	6%	-13%	-2%	8%
	Investment Grade Corporate Bonds	3%	-3%	5%	-20%	-4%	8%
	High Yield Corporate Bonds	3%	2%	5%	-15%	0%	-1%
Alternatives	Commodities	3%	0%	-13%	14%	27%	-4%
	Gold	26%	27%	13%	-1%	-4%	25%
	Bitcoin	14%	115%	156%	-64%	58%	302%

Source: Bloomberg (7/1/2025)

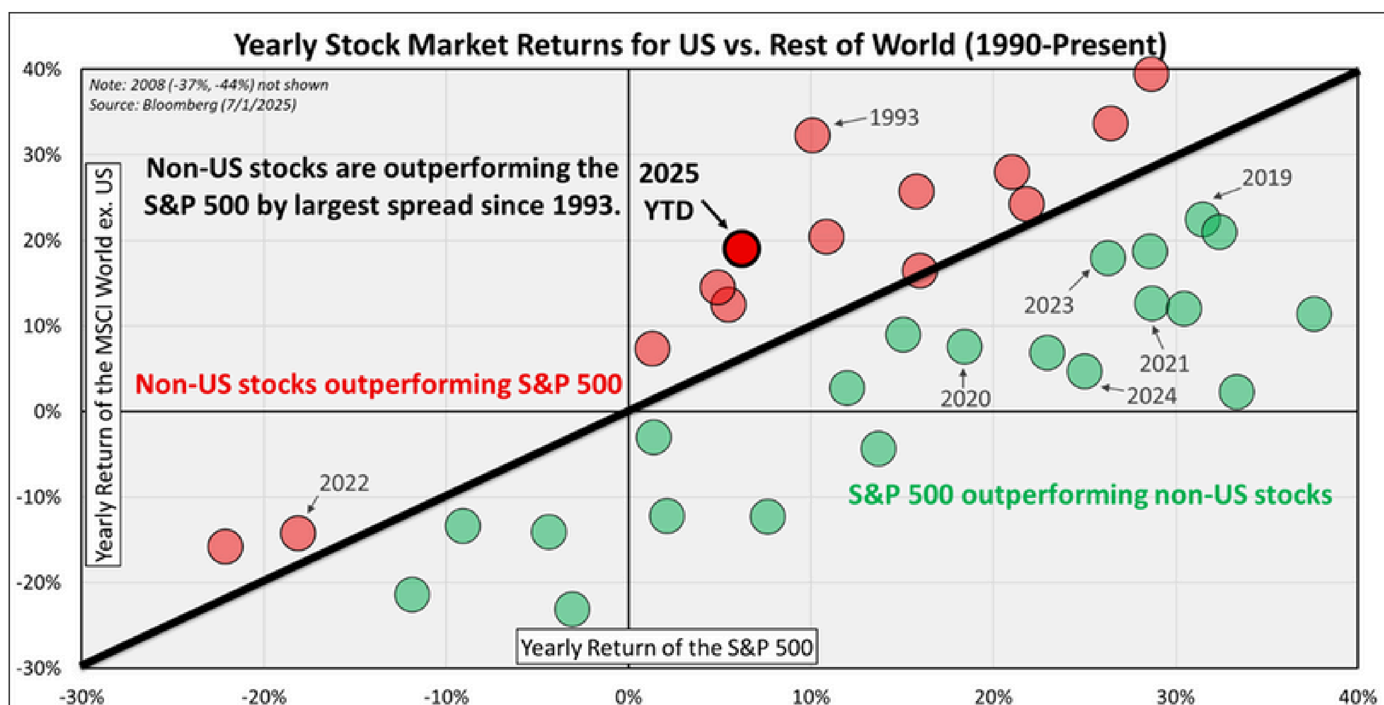
Through the first half of 2025, US stocks provided mostly positive returns. However, other areas of the world, and other asset classes, provided significantly higher returns.

For the first time since 2021, US growth and value stocks posted similar returns after two years of growth stocks significantly outperforming value stocks.

US mid and small cap stocks continued to underperform, with mid cap stocks flat and small cap stocks losing value over the first 6 months, while US bonds provided returns between +3 to +4%.

Gold continued to outperform all asset classes returning +26% in just 6 months. These returns are on top of the +27% returns in 2024 and +13% in 2023.

International Stocks



For the first time in 22 years, international stocks outperformed US stocks by more than 10%. As shown in the chart above, over the past 35 years, US stocks have outperformed global stocks 60% of the time (the yearly dots are colored green if US stocks outperformed that year, and red if international stocks outperformed). US stocks have also outperformed international stocks in 5 of the last 6 years.

That script flipped the first six months of 2025 with international stocks outperforming the US by the largest margin since 1993 with global stocks, ex-US, returning +18% while emerging market stocks returned +15%.

At DSG Capital Advisors, we have been monitoring the outperformance of international stocks and believe non-US markets could provide positive returns in the second half of 2025. In order to identify attractive opportunities within international stocks, we have expanded our quantitative algorithms to include many of the largest international companies. We anticipate continuing to add select international stocks to our portfolios as market conditions warrant.

Sector Performance

Percent of the S&P 500	Sector	1H 2025	2024	2023	2022	2021	2020
8%	Industrials	**13%**	17%	18%	-5%	21%	11%
10%	Communication Services	**11%**	40%	56%	-40%	22%	24%
2%	Utilities	**9%**	23%	-7%	2%	18%	0%
14%	Financials	**9%**	31%	12%	-11%	35%	-2%
33%	Information Technology	**8%**	37%	58%	-28%	35%	44%
6%	Consumer Staples	**6%**	15%	1%	-1%	19%	11%
100%	**S&P 500**	**6%**	**25%**	**26%**	**-18%**	**29%**	**18%**
2%	Materials	**6%**	0%	13%	-12%	27%	21%
2%	Real Estate	**4%**	5%	12%	-26%	46%	-2%
3%	Energy	**1%**	6%	-1%	66%	55%	-34%
10%	Healthcare	**-1%**	3%	2%	-2%	26%	13%
10%	Consumer Discretionary	**-4%**	30%	42%	-37%	24%	33%

Source: Bloomberg (7/1/2025)

Sector performance for the first six months of 2025 was directionally the same as 2024 with a few notable exceptions.

A new sector emerged as the best performer during the first 6 months of 2025 -- Industrial stocks lead the way with the sector returning +13%. Analyzing data back to 1990, this is the first time that the Industrial sector was the best performing sector over the first 6 months of the year. Additionally, Industrials have never before been the strongest sector on a full-year basis. Howmet Aerospace, one of our portfolio holdings discovered through our quantitative screening process, was the top performing Industrial company returning +70%. In fact, Howmet was the third best performing stock in the S&P 500 for the first half of 2025.

Technology companies fell from second place in 2024 to 5th place in 2025. It is worth noting, however, that the Technology sector's performance was stronger than the overall market following the April 8th low.

Consumer Discretionary had the largest decline, falling from fourth place in 2025 with +30% returns to last place for the first six months of 2025 with -4% returns. Keep in mind that the "Mega caps" Amazon and Tesla dominate sector level performance – Tesla's -17% YTD and Amazon's flat first half dragged the Discretionary sector's performance down.

Finally, Healthcare stocks continue to struggle. After returning only +3% in 2024, Healthcare stocks lost -1% for the first six months of 2025. There is nuance in most things investments – sector performance being no different. The Healthcare sector has suffered shifting regulations and lack of exposure to key market themes such as robust economic growth and artificial intelligence.

S&P 500 P/E Multiples

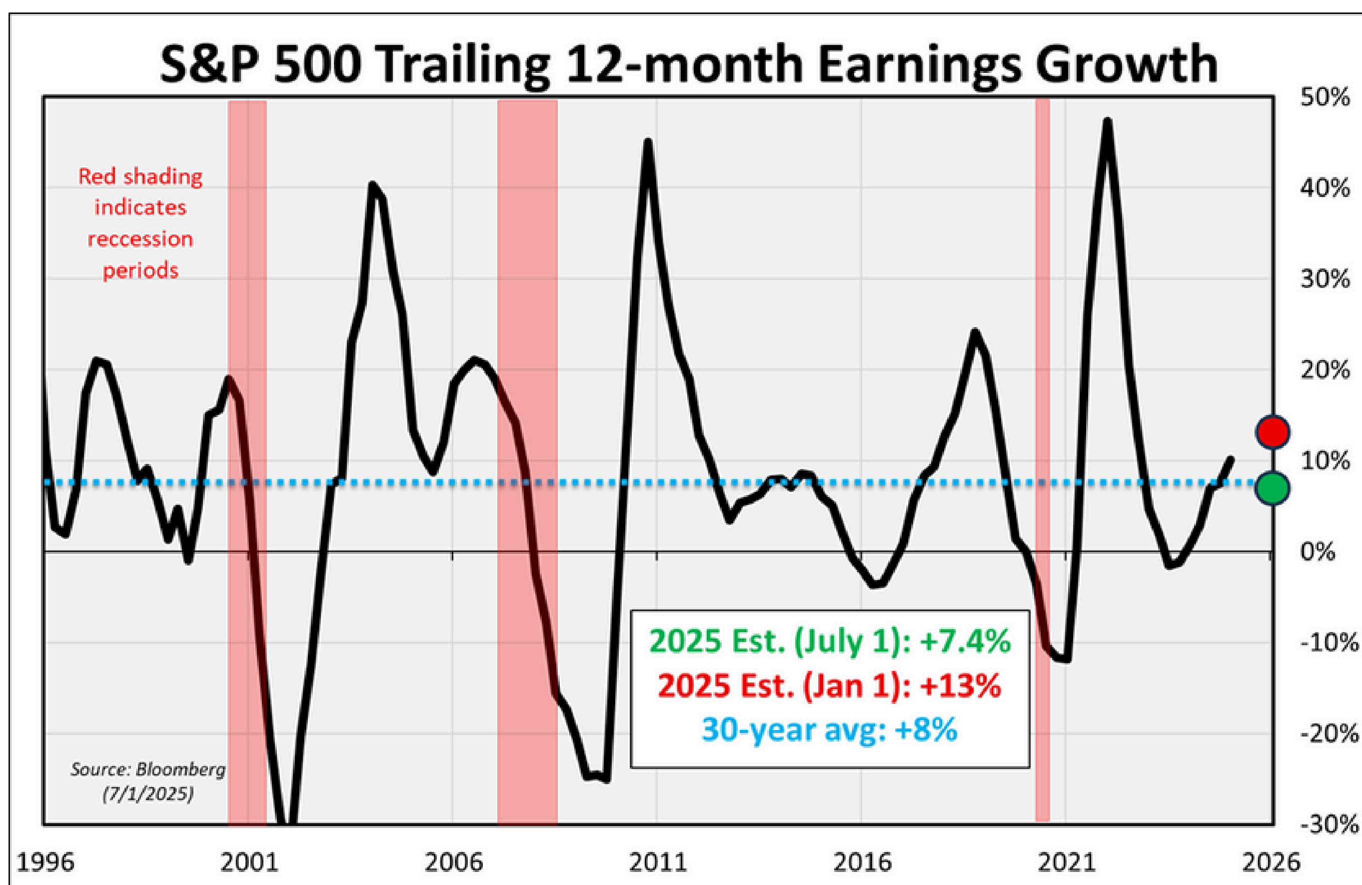
Given the outsized returns in 2024, many investors were focused on elevated stock valuations. As shown in the chart above, the S&P 500 Index ended 2024 with a forward P/E ratio of 21.7x, more than one standard deviation above the historic averages and significantly above the 30-year average of 16.9x.

After a brief decline to 20x P/E on the “tariff” tantrum, stocks ended Q2 2025 with a P/E multiple of 22x. This means that much of the S&P 500’s first half 2025 returns can be attributed to further multiple expansion rather than earnings growth. The elevated multiples of today draw parallels to the late 1990’s.

As we have witnessed throughout history, elevated stock prices eventually need earnings growth to maintain those valuations. Put simply, high stock multiples without earnings growth are not sustainable over the long term.

With a backdrop of extended valuations, we are leveraging our quantitative algorithms to identify companies with a blend of both robust growth potential and reasonable stock multiples.

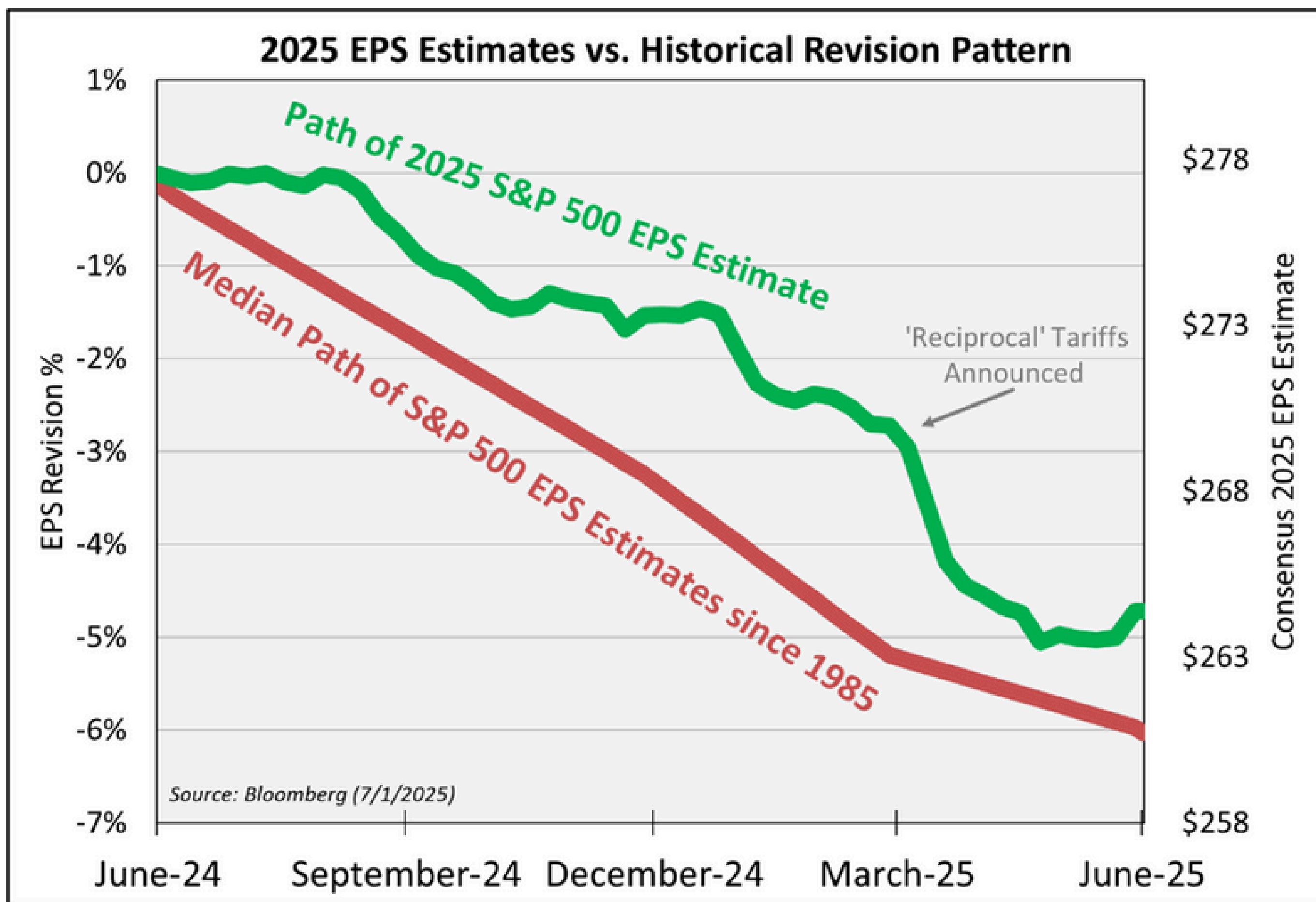
S&P 500 Earnings Growth



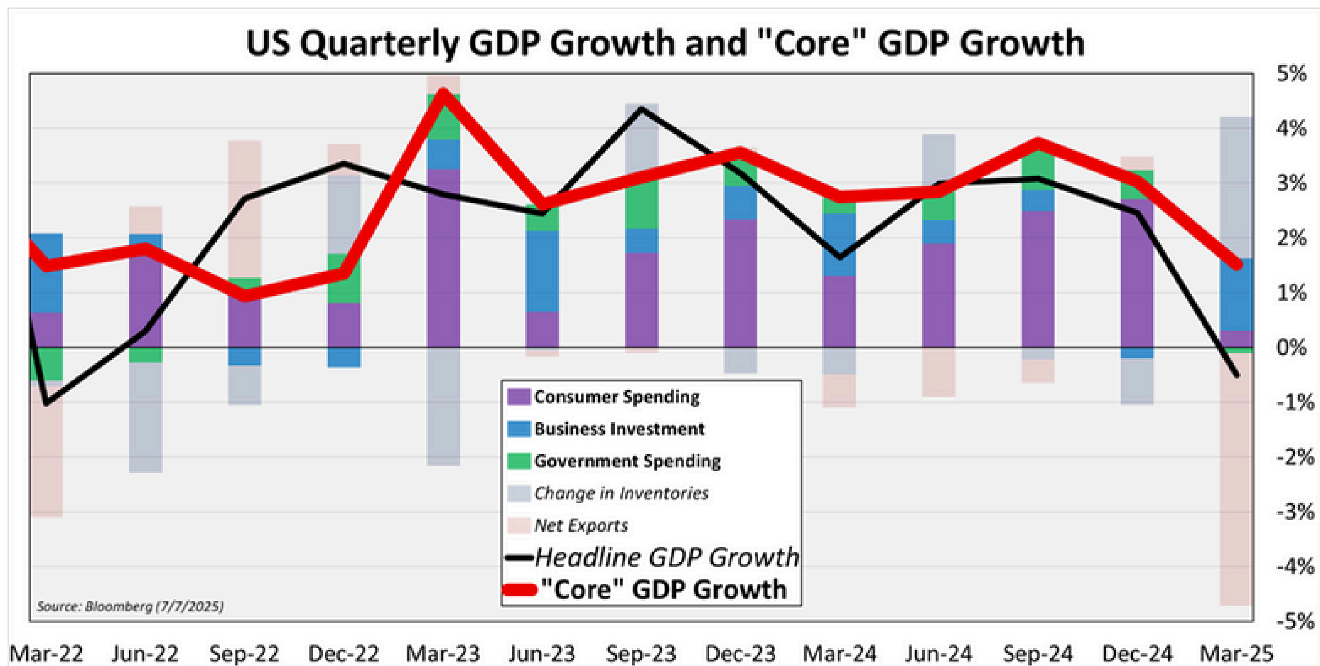
Investors started 2025 with earnings growth estimates of +13% for the year. This was significantly above the 30-year average annualized earnings growth rate of +8%. The current estimates for 2025 earnings growth rate have fallen to +7.4%, mirroring the S&P 500's 2024 earnings growth rate.

As shown in the chart below, it is not uncommon for analysts to downwardly revise earnings growth expectations throughout the year. In fact, since 1985, the median downward revision to S&P 500 EPS estimates through the first half of the year has been -6%.

It should be noted that the 2025 downward revisions to earnings estimates in 2025 were much better than the historical -6% median decline until the reciprocal tariff policies were announced in April. Despite the tariff-related declines, negative revisions have subsided and remain modestly above historical averages as we head into Q2 earnings season.


2025 EPS Estimates vs. Historical Revision Pattern
Path of 2025 S&P 500 EPS Estimate
Median Path of S&P 500 EPS Estimates since 1985
'Reciprocal' Tariffs Announced
EPS Revision %
Consensus 2025 EPS Estimate
1%
0%
-1%
-2%
-3%
-4%
-5%
-6%
-7%
$278
$273
$268
$263
$258
June-24
September-24
December-24
March-25
June-25
Source: Bloomberg (7/1/2025)

U.S. Economic Growth



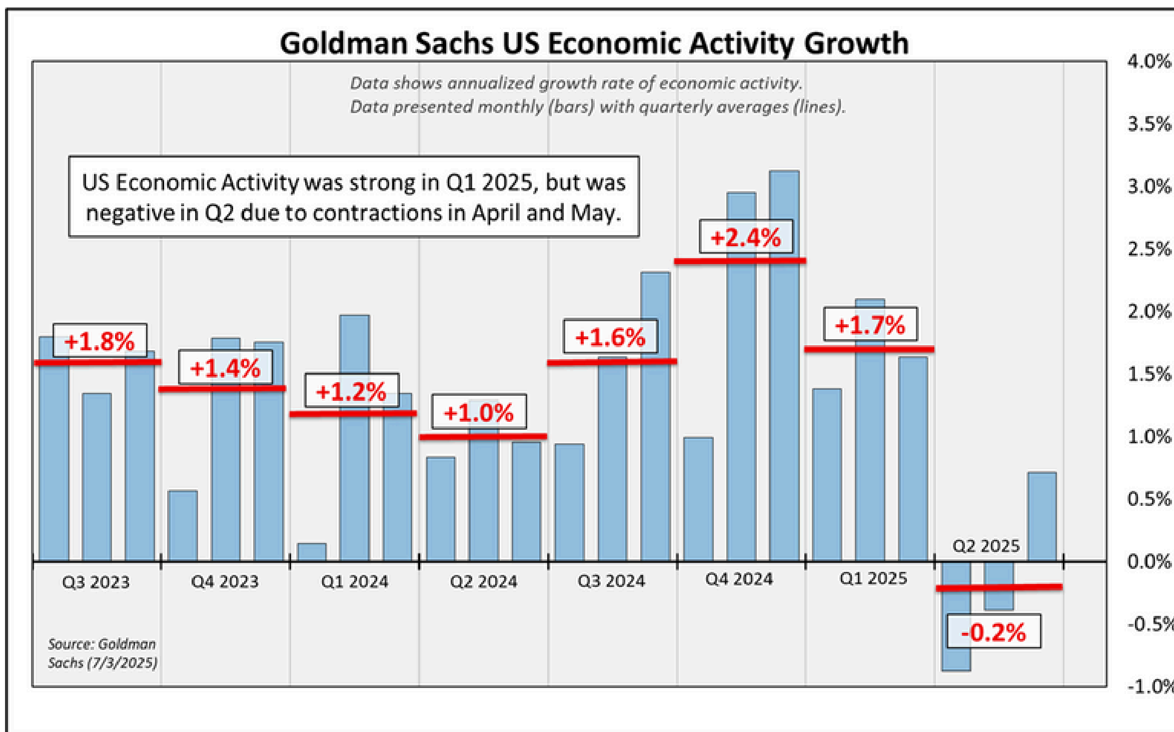
It is commonplace for analysts to use GDP as the primary measure of US economic growth. Analyzing GDP data, however, can be complicated due to the numerous components and the number of revisions.

The first quarter GDP figures are a prime example of why the data must be carefully analyzed and interpreted to formulate an opinion on what the data is signaling. As shown in the chart above, the first quarter data indicated that the US suffered a -0.5% GDP growth rate decline. While this figure is technically accurate, we think it would be a mistake to interpret this as an economic contraction.

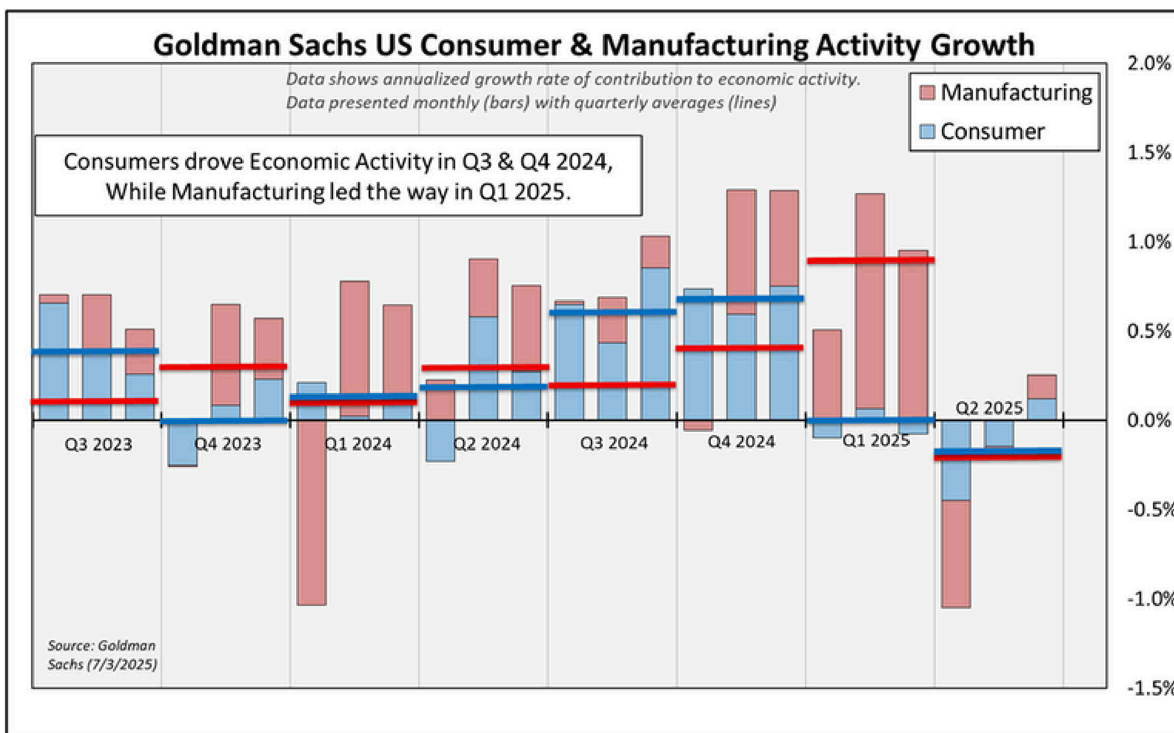
Our rationale stems from how GDP is calculated – namely the inclusion of exports, imports, and inventories. In Q1, companies imported an unusually large amount of goods to avoid the impact of possible tariffs. The amount of imports caused the GDP growth figure to decline by -4.6.

Simultaneously, the stockpile of inventories added +2.6% to overall GDP growth. Both of these occurrences were idiosyncratic instances caused by the sudden onset of the tariff policy. We would categorize these distortions as technically accurate, but not reflective of the underlying economic growth trends.

To offset these distortions, we constructed a "Core" GDP figure that includes Consumer Spending, Business Investment, and Government Spending –- what we believe to be a more accurate reflection of the economic signal underlying GDP data. "Core" GDP advanced +1.5% in the first quarter as seen in the chart above. The figure is well below +3.5% GDP growth rate of 2023 and +3.1% growth rate in 2024, but significantly above the -0.5% headline GDP number.



Another way to measure economic growth is to take a broader measure of economic growth. The chart above from Goldman Sachs represents their measure of the economic activity data. As shown in the chart above, US Economic Activity posted a solid +1.7% increase in Q1 2025 (similar to our "Core" GDP growth figure of +1.5%), but declined in Q2 to -0.2%, likely driven by tariff uncertainty.

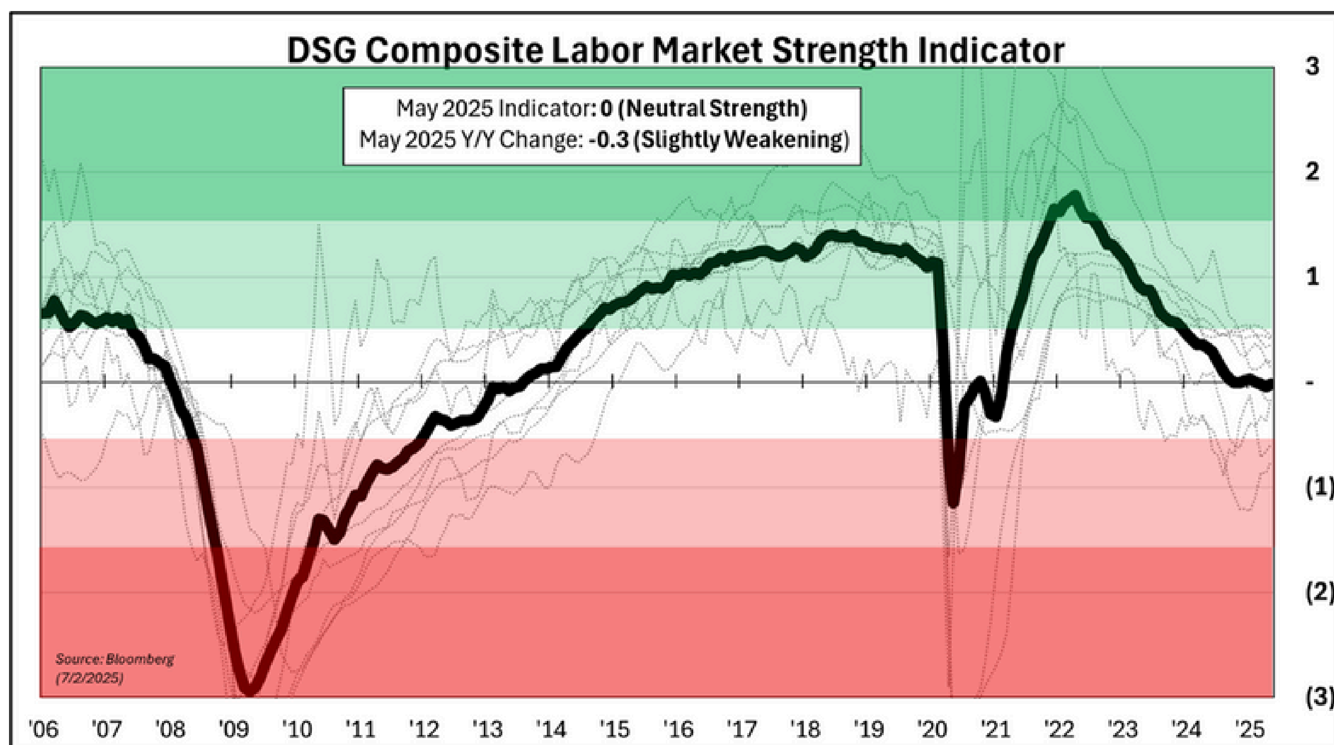


Finally, as shown in the chart above, while consumers drove economic growth in the second half of 2024 (blue bars), manufacturing took over in 2025 (red bars).

At DSG Capital Advisors, we believe the certainty of a tax bill, combined with significant progress on tariff policy, could position the US for further economic expansion. In fact, we interpret the market leading performance of industrials – for the first time in at least 35 years – as a sign that investors are anticipating US economic growth can regain its footing.

We will be analyzing earnings reports from industrial companies closely during Q2 earnings season. While tariffs slowed economic activity in April and May, we are optimistic that the strong Q4 2024 and Q1 2025 manufacturing data will provide enough support to sustain strong manufacturing momentum for the second half of 2025.

Labor Market



The strength and resilience of the US labor market was a defining feature of the post-COVID economy. Despite inflationary pressures, consumers proved to be the driving force behind economic expansion in 2023 and 2024. A strong labor market was the driving force behind a strong consumer.

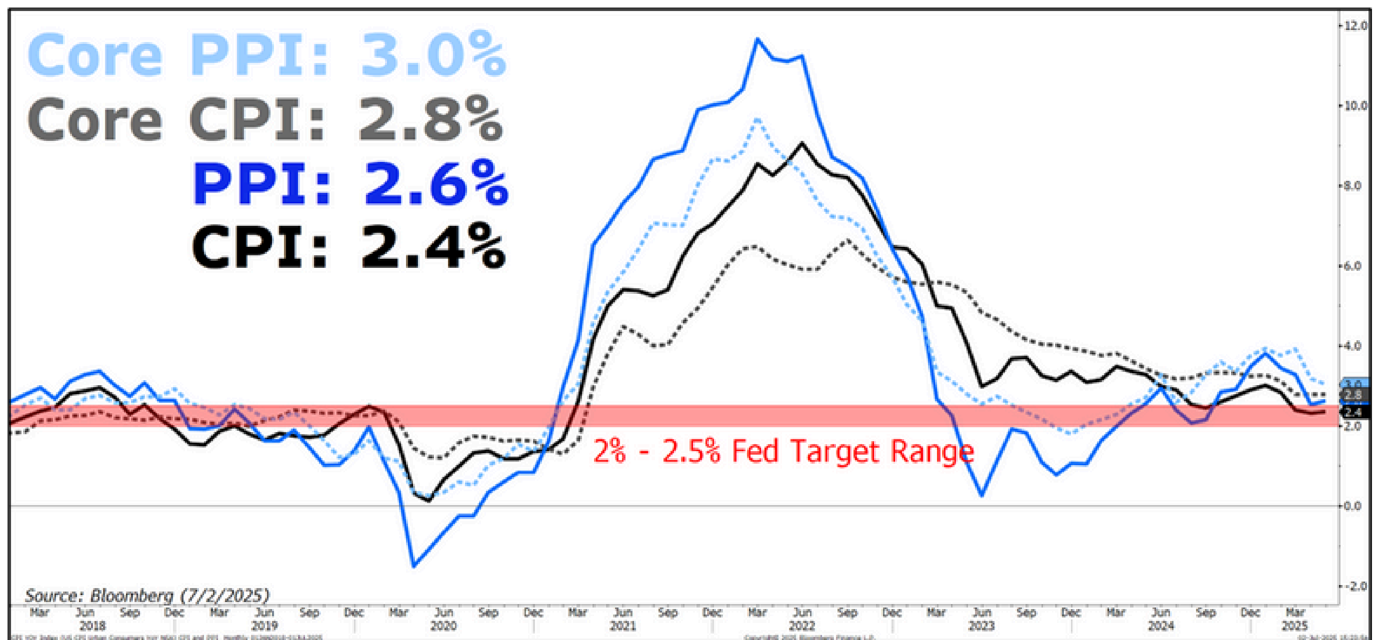
Tracking labor market data can prove difficult for investors. There are a variety of datasets and methodologies that can provide conflicting signals. To address this issue, we analyze a variety of key labor market indicators and combine them into a composite score to gauge the aggregate health of the US labor market.

Our composite score is indicating that the US labor market has been weakening from a place of remarkable strength over the last three years, and now rests at a roughly neutral level of strength. Importantly, the negative rate of change has slowed over the last year, with the labor market only slightly weakening.

This is important because a defining feature of a recessionary environment is a labor contagion effect – where weakness begets more weakness and accelerates downward. Over the past year, the glidepath for the labor market has been only slightly lower, and has been generally stable over the past several months.

How the labor market performs from this neutral position is a critical piece of data that will influence economic growth, and stock performance, in the months and quarters ahead. Layoffs and policy cuts have driven a pullback in public-sector hiring. More restrictive immigration policies could put further pressure on labor market growth. Ultimately, the labor market will depend on the durability of the US economy and the ability of US companies to earn sufficient profits in a post-tariff regime where they are not compelled to reduce jobs to maintain operating margins.

Inflation



Inflation continued to decline in the first half of 2025 with CPI falling from 2.9% to start the year down to 2.4% in May. As seen in the chart above, Headline CPI, Core CPI and PPI all currently reside between 2.4% and 3%. This is good news for investors as inflation appears to be stabilizing.

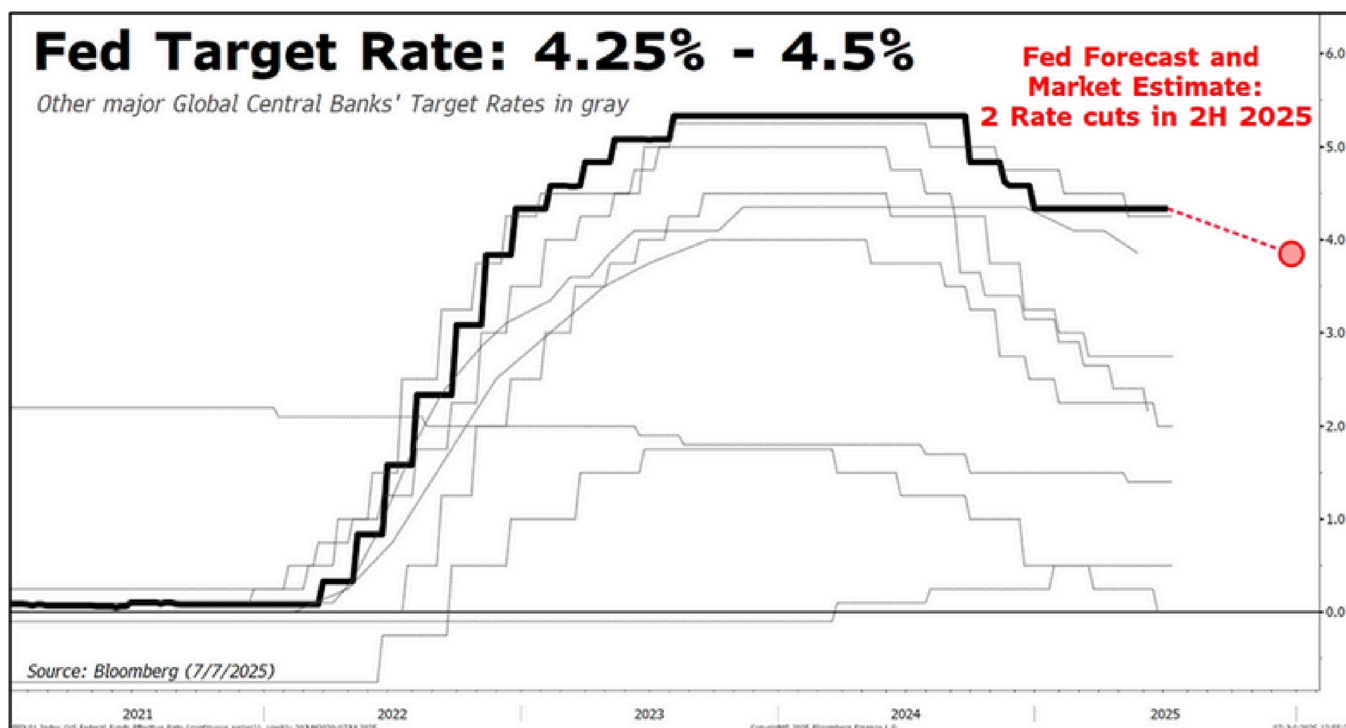
As we wrote in our 2025 Outlook, higher but controlled inflation around 3% could help the US address its ballooning debt issue by devaluing the impact of the debt over time.

Despite the benign current reading, the Federal Reserve is on high alert for any tariff-induced inflation. Historical research suggests that a portion of tariff costs may be passed on to consumers. Ultimately, the cost of tariffs must be paid – whether the cost is paid by the manufacturers and suppliers of the goods, the companies selling the goods, or the consumers purchasing the goods, someone is going to incur the costs. How the costs of the current tariff policy are absorbed is yet to be seen.

In our 2025 outlook, we posited that investors could navigate potential inflationary pressures by 'outgrowing' the inflation, and we continue to believe that to be the case today. As we stated in our 2025 outlook:

> *"[With fiscal] policy that attempts to spur economic growth by creating higher economic output, wages, interest rates, bond yields and inflation, we think investors should consider investing in assets that "outgrow the problem." In this scenario, we would encourage investors to consider investing in high growth companies whose revenues and earnings provide real growth, meaning they grow faster than the rate of inflation."*

Monetary Policy



After a series of rate cuts in late 2024, the Federal Reserve left rates steady for the first half of 2025. The Fed is currently operating under difficult conditions with the uncertain economic impact from tariffs and how they could impact inflation and the labor market in the future.

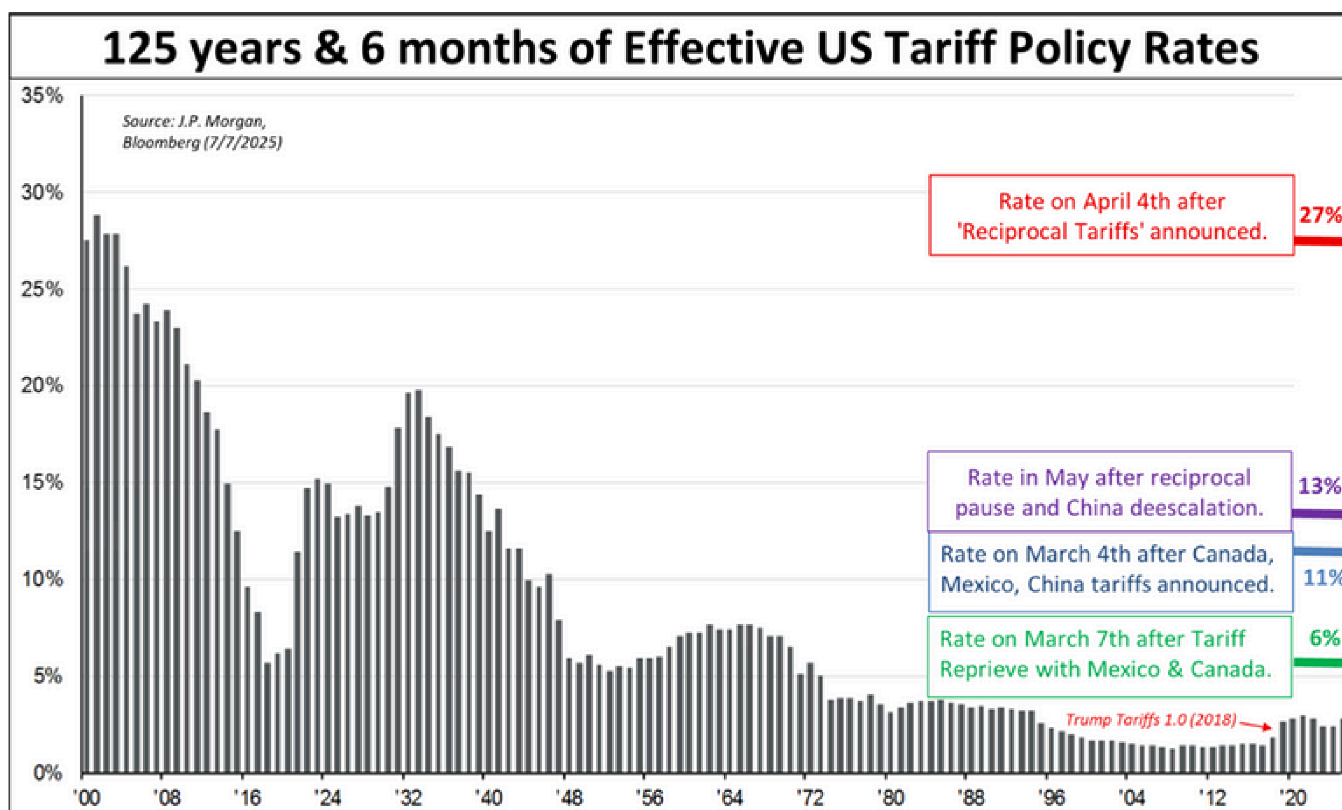
As a result, the Federal Reserve has been reluctant to make abrupt changes. In the words of Powell, "It's kind of common sense thinking that when the path is uncertain, you go a little bit slower... It's not unlike driving on a foggy night or walking into a dark room full of furniture; you just slow down."

The Federal Reserve has forecast that they will cut interest rates twice before the end of 2025. Currently, investors appear to be aligned with this forecast.

Historically, elevated inflation has caused the Federal Reserve to raise interest rates, while elevated unemployment has caused the Fed cut rates. Should inflation remain benign, the Fed may have room to modestly cut rates in an attempt to protect a gradually weakening labor market. If labor market weakness escalates, however, the Federal Reserve may cut rates more aggressively than currently forecast.

The Federal Reserve and Chairman Powell have come under increasing scrutiny from the White House, with President Trump publicly criticizing Powell for not cutting interest rates faster. The Fed’s dual mandate is maintaining maximum employment and stable prices – even if the pursuit of these goals is viewed to be at odds with Executive Branch desires.

Tariffs



Entering 2025, investors were aware that tariffs were a component of the Trump Administration agenda. Many were looking to Trump 2018 trade war with China (Trump 1.0) – which was generally narrow in scope – as a guide for Trump 2.0's tariff framework.

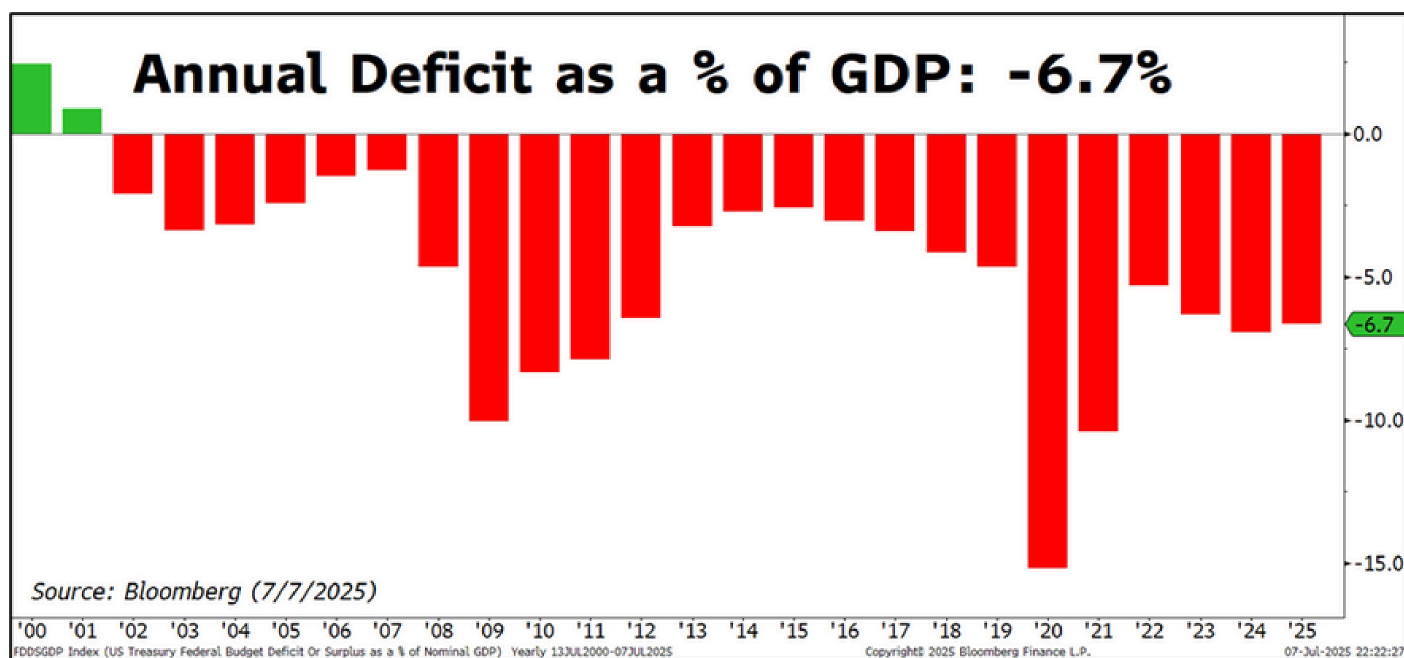
Instead, tariffs were levied against most of the world's trading partners and across most categories of imported goods. The 'Reciprocal Tariff' policy rollout in April proved to be a powerful force of economic volatility and instability.

The chart above highlights a few key levels from earlier in the year and compares them to effective US Tariff Rates over the last 125 years. It is no wonder that investors, consumers, companies and the Federal Reserve were uncertain about the economic path forward.

Current estimates place the new US effective rate at roughly 13%. This change would be more than double any other year-to-year change in history and would impact decision making across nearly every component of the economy.

While the final implementation of tariff policy has yet to occur, we think it is important to note that tariff policy uncertainty has declined as the Administration secures agreements with major trading partners. Should the Administration continue to offer more clarity and consistency with its foreign trade policy, companies and consumers should be able to better plan for the potential impact of the new tariff policies.

U.S. Fiscal Debt



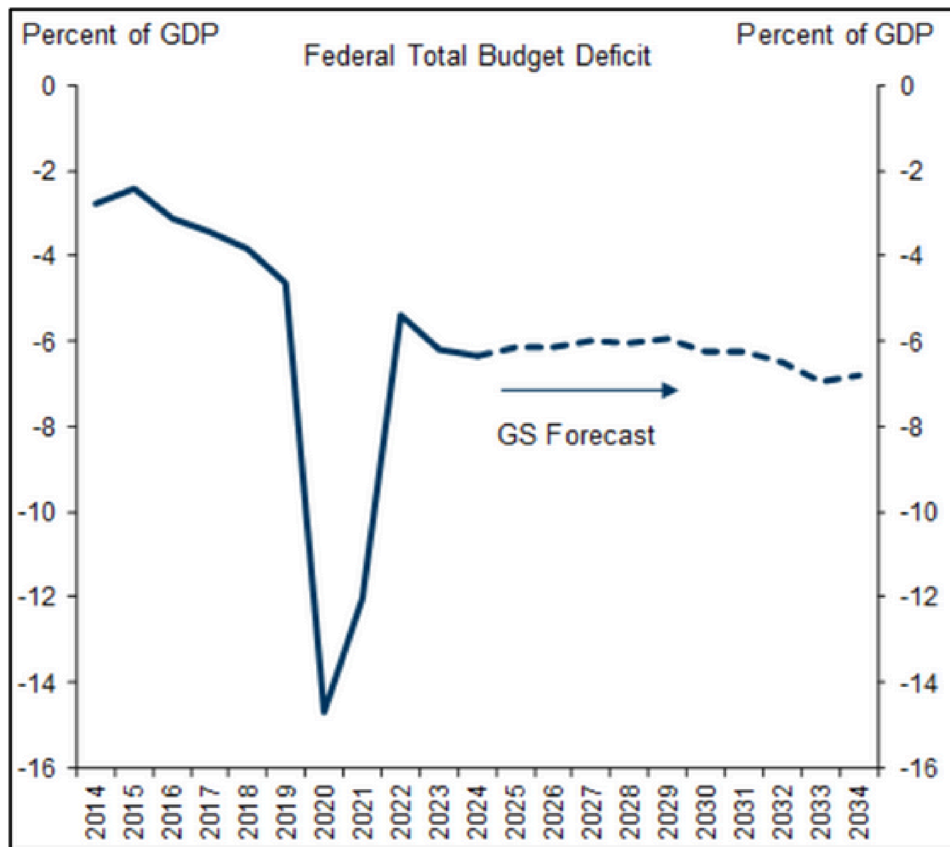
As we discussed at length in our 2025 outlook, we continue to believe that the persistent US Government deficit remains one of the largest long-term financial issues for the United States.

As seen in the chart above, the Federal Government continues to run significant budget deficits, even after adjusting for economic growth. The current deficit is -6.7% of GDP and the last 6 years have been the six highest deficit / GDP years since World War II.

This means that the Federal Government continues to spend more money than it makes. In our 2025 outlook, we wrote that the problem would not be easy to solve. We suggested that a potential solution would center around a period of controlled spending while simultaneously increasing revenues:

> *"In our opinion, the most plausible option is for the U.S. Government to take a hybrid approach that involves decreasing spending and increasing revenues (i.e., through higher taxes and tariffs) to reduce the size of the annual budget deficits going forward."*

We were hopeful that the new Administration was up to the challenge, and certainly the messaging out of the Administration indicated a desire to stabilize the debt issue.



Source: Goldman Sachs (6/17/2025)

The chart above shows Goldman Sach's forecast of the US deficit as a percentage of GDP for the next 10 years. The passage of the Big Beautiful Bill appears to reinforce that the Trump Administration is planning to continue the deficit "status quo." Goldman forecasts that the current deficit as a percent of GDP won't materially expand but also won't materially improve, either. This means that even after accounting for economic growth, the US will continue to add to its net debt at a yearly rate not seen since World War II.

The question to be answered is what level of budget deficits will actually materialize and how is that going to affect future fiscal and monetary policy.

Conclusion

After 2 consecutive years of 25%+ returns for the S&P 500, investors wondered how stocks would perform in 2025.

At the start of the year, we indicated that we thought stock returns for the US would be driven by six themes: (1) US debt levels, (2) New Administration policies, (3) Federal Reserve and interest rates, (4) Inflation, (5) AI transitioning from “build out” to “implementation,” and (6) Corporate earnings growth.

At the time of our writing, we had no idea how impactful some of these themes would be during the year. Specifically, the New Administration’s tariff policies turned global trade policies upside down. The rollout of the tariff policy projected a high degree of uncertainty into US and global financial markets. Stock markets reacted as they often do when volatility spikes -- the S&P 500 fell more than -10% in 48 hours.

The selloff proved to be brief, however, as President Trump eventually indicated the tariff policy implementation date would be delayed and stock markets rallied back to all-time highs within a matter of 3 months.

Following this announcement, and significant progress on a tax bill, investor outlook has grown more optimistic. The economic ramifications of the inconsistent tariff policy rollout, however, are yet to be discovered. Specifically, the final size of the tariffs, and who bears the economic burden among suppliers and manufacturers, companies or consumers are yet to be determined.

Nevertheless, as we enter the second half of 2025, inflation rates are declining, the labor market remains broadly stable, and corporate earnings projections are in line with the 30-year average.

Without a clear economic path forward, the Federal Reserve remains on the sideline… at the chagrin of the President. Although the Federal Reserve has projected two rate cuts during the second half of 2025, we are mindful that the cuts are highly dependent on stable inflation and labor markets.

All in all, despite a lot of uncertainty and volatility, the first six months of the year have been fairly productive for investors. US stocks and bonds have provided low-to-middle single digit returns. International stocks have taken the lead with double digit returns. With elevated US stock multiples, international stocks could continue to outperform for a period of time.

Heightened global volatility and uncertainty caused gold to continue to rally and return an incredible +26% during the first six months, nearly matching its full year return last year.

At DSG Capital Advisors, absent escalating geopolitical tensions, we believe 2025 could turn out to be one of the rare occurrences where stocks end the year positive after two consecutive +25% return years - an occurrence that has only happened 4 times over the last 100 years. We anticipate 2025 will enter the history books as the fifth occurrence.

DSG Capital Advisors

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