

Fidelity Viewpoints[®]: Market Sense

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TRANSCRIPT

SPEAKERS:

Heather Hegedus Jurrien Timmer Yasmin Landy

HEATHER HEGEDUS: Hey there, everybody. Thank you so much for making the time to join us today for *Market Sense*. I'm Heather Hegedus with Fidelity. So this week could be a pivotal week for the markets and economy. And it's already shaping up to be as we speak.

So the Fed is meeting right now as we speak. It's also a peak earnings week with some Mag Seven mega-cap companies reporting earnings tomorrow and Thursday. And some key indicators on the state of the economy are coming this week as well, including another inflation report.

And then just as we were coming on the air right now to you, we got news about the Chinese trade negotiations as well. And you may know, a trade deal was reached with the EU over the weekend as well.

And the markets are increasingly bullish. The S&P is down today. But last week, the S&P recorded new all time highs on a daily basis. And right now, it's on track to close out this month as its fourth month of consecutive gains.

So as always, we've got a lot to talk about, but especially this week. And to hear his thoughts on how investors might be thinking about all of that, we are joined today by Jurrien Timmer, who's Fidelity's Director of Global Macro.

Plus, today, we are delighted to welcome back Yasmin Landy, who is an institutional portfolio manager here at Fidelity. She focuses on international stocks. And we have been getting a lot of questions from you at home on what kinds of international stocks you might want to consider, and how much exposure you might want to allocate to them.

And Yasmin is going to be getting us caught up on the latest global developments today, and talk about where there may be future opportunities in that space as well.

So, thank you, both of you, for making the time to be with me today, on what is shaping up to be a pretty busy newsday.

YASMIN LANDY: Thanks so much for having us. It's great to come back on.

JURRIEN TIMMER: Nice to see you both. Welcome, Yasmin.

HEATHER: All right, let's get this started. It's Tuesday, July 29. It's our last show of July. Can you believe it? July just flew by.

As I mentioned off the top, shortly before we came on the air, US and Chinese negotiators concluded their latest round of trade talks in Stockholm with an agreement to extend that tariff pause with China.

I was just listening in on that news conference hearing with Treasury Secretary Bessent, and US Trade Representative Greer, who said the plan technically does still need to be brought to the president, to the Oval Office, which will happen tomorrow for his sign-off. But it sounds like things are on track here.

And then the big headline from over the weekend was the US trade deal with the EU. Just like with Japan, a 15% tariff was announced on most European imports.

That China news comes three days before that August 1 tariff deadline. So given all these things together, Jurrien, is it now safe to say that that tariff-related market volatility from earlier this year could be nearing an end?

JURRIEN: I think certainly the wave of the tariff tantrum appears to have crested, because we're getting more and more deals, and they're all in that 15% range.

And of course, 15% is bigger than 0. And someone has to pay for this. This is basically an import tax, or a VAT tax, like they have in Europe. And it's still unclear as to who pays. Is it the consumer through higher prices? Is it the importer through lower margins? Is it the exporters through better trade arrangements?

To what degree does it even get offset by currency movements? So it's not a cut and dry topic. But I think, considering where we were on April 2, when we saw that big billboard with all of those big tariffs on them, something in the 15% area, I think, is something the market can live with. And that's what we've seen in the price action.

And of course, some of that in terms of its impact on earnings could very well be offset by the Big Beautiful Bill.

So you have to always look at all the moving parts, and see to which degree they either offset each other or amplify each other. And in this case, you have a lot of cross-currents. And the tariffs is only one of them.

But I think, at this point, with the Big Beautiful Bill being signed into law a few weeks ago, and the tariff wave, again, maybe going back out to sea little bit, I think the market's on a footing where it has a sense of what's coming.

And markets don't like uncertainty. And so if we get more visibility, that helps companies plan. It will help them guide estimates. And that's what we're seeing now.

HEATHER: Certainly, been a busy July right. We had the Big Beautiful Bill signed into law, as you said. These tariffs negotiations. So it has certainly had not been a slow summer by any means.

I want to switch gears here, and ask you about a totally different topic now. Last week, we saw a revival of trading activity in meme stocks, which drove rallies for a handful of companies.

Of course, this is when individual traders make bets based on online personalities, endorsing particular stocks, lower performing stocks.

We saw this meme stock craze back in 2021, of course, with GameStop. Folks might remember that, with Roaring Kitty. What is this telling us about the market right now? And do you see any potential danger to this?

JURRIEN: So the meme stock frenzy from 2021. So, nonprofitable tech stocks, like you said, GameStop, AMC, very speculatively-oriented trading, was de rigueur back in '21. And of course, we had very easy money back then.

So we had, obviously, COVID. Then came the \$5 trillion fiscal stimulus. And the Fed, of course, was amplifying that, or absorbing that stimulus through lower rates, zero rates and quantitative easing.

And I think most people would probably agree that the Fed stayed too accommodative too long. And that usually, or often, will cause overt speculation, when there's too much liquidity sloshing around.

And of course, back then, people were stuck in their homes, and there were no sporting games, so they had to do something.

So that was 2021. And that bubble burst in 2022, when the Fed raised rates significantly. So the Fed, of course, is not doing that right now. It's cutting rates, or it has cut rates, modestly, last year.

And of course, the Fed is meeting this week. And we'll see if they do it some more. The chances are, that they won't yet. But I think what the market is doing is, we were in a fearful place in April, staring into the abyss, if you will.

Now, the markets have been making new all-time highs almost on a daily basis. That gets people more confident. And you see the sentiment swing from fearful to complacent to maybe a little bit too confident.

And I think with the fiscal bill coming in, more money out there out there to be spent, and potentially the Fed cutting rates in the future. And of course, that's become a political debate as well. I think "animal spirits," those speculative sentiments have come back, and you're seeing some of those stocks come back to life.

If that's an entertainment thing for people wanting to trade or gamble, who am I to judge? But to me, that's not investing. It's gambling. It's entertainment. Might as well go to a Casino. But that's just me.

HEATHER: Animal spirits, meaning people climbing that wall of worry, and making decisions not necessarily based on fundamentals?

JURRIEN: I mean, people feeling more confident about taking risks.

HEATHER: Is there a danger to that?

JURRIEN: Well, in '21, you saw that it went to extremes. Not only with the meme stocks, but crypto. And so when that liquidity spigot gets turned off, as it did in 2022, if those companies don't have a real underlying value, then that bubble pops. And so that's always the risk.

HEATHER: All right, Jurrien. Thanks for getting us caught up on the latest headlines. I want to turn things over to Yasmin, to make sure we have enough time for her to talk about international stocks.

And as I mentioned, Yasmin, we've been getting a lot of interest from *Market Sense* viewers, writing to us every week, asking about potential opportunities in this space, given the big shift this year that we saw with international stocks vastly outperforming US stocks.

First of all, can you talk about what you see to be happening here, and if you think this trend has longevity? Do you think this is going to last, Yasmin?

YASMIN: It's good to hear that people are reaching out and asking about this. So we had a good stretch pre the global financial crisis, where you had the Ascension of China, and the non-US markets were doing really well. EM was taken off, and that brought along Europe, and other places as well.

So post-GFC, we've gone through a stretch where we're underperforming the US markets. And I think those of us who are following the markets will see that the S&P is about up 8.7% year to date, as of yesterday.

And for the non-US markets, developed markets are up about 20%, really driven by Europe. And EMS up 18.6. So really strong results. And that's in US dollar terms.

So this has been exciting for the investor in the US who has decided to allocate to the non-US. Because finally, diversification is paying off.

So to your question of will this last, and what's happened. There's a couple of things that I would note. When you look at some of the flows, just like we have home country bias, when things start to get on the rocks, where we'll bring our assets back home to the US, the same thing happens abroad.

And when you have a policy uncertainty, you saw that happening where the flows were returning to home country, Europeans pulling dollars into the European market.

And so you really saw this reversal of flows coming out after a long time of interest in the US market from Japanese investors, European investors, across the globe.

So what is the setup today? In the beginning of the year, I would say, you really need to look for three things. You need to look for valuations, and then a catalyst, something that is going to change the dynamics. Those would be fundamentals. And then we'll talk a little bit about currencies.

So, for valuations, at the beginning of the year, there was about a 40% disparity between the US and the non-US in terms of valuations. So this setup really well. Because usually you had a long period of time where the non-US markets were getting cheaper versus the US markets.

And there is a point where you have to pay attention to it. But usually you need a spark. You need something that's going to trigger recognition of the cheapness of another market. And that's where I think the fundamentals came in.

So very high-level, big picture thinking. You've gone through a period of time, post a great financial crisis, where Europe was really in austerity mode. You may remember the Greek crisis in 2012. The name of the game was not fiscal spending.

And through the shift in policy, in the dynamics between countries, I think there's a really true shift where, in particular, Europe is loosening the purse strings, as you can see from Germany's change in fiscal policy, where they want to both take the reins in terms of their own defense. And also, I think, I would put in the category of growth, and making sure that their companies are healthy as well, and trying to be a little bit more competitive in other policies vis a vis the US.

The other thing that's shifted is the backdrop in terms of rates. And this has allowed the financials, the banks in the region to become much more healthy. And this was something that really kept a lid on growth and health of the market, particularly in Europe.

And now you have a much better backdrop. You have a very well-funded financial system. And right now, that means that they've been giving dividend payouts. They've been buying back stock shares. But at some point, it's likely that lending will also pick up. And that could be helpful.

If other countries outside of Germany also start to spend a little on the fiscal side, that also is really helpful. And then currency has certainly been a tailwind.

HEATHER: Let's talk about currency. You talked about valuation and fundamentals, both contributing to positive returns overseas. But let's talk about currency. How is a weaker dollar affecting international markets, Yasmin?

YASMIN: Yeah, sure. So from the first point is, really, if you're a US-based investor at the stock level, converting those stock shares back into USD, you're going to get an uplift in your investment right there.

However, I think you need to be important on the fundamental company side. Because for some companies, a weakening currency can be actually a headwind. If you think about companies that have a lot of their revenue and US dollar, like a European pharma company. That can be a headwind.

So we're always looking at the currency of cost versus the currency of revenue. So that's pretty key.

The other thing that I would note is, it was often thought that a weakening dollar was a real big tailwind for emerging markets. However, the composition of emerging markets has shifted a lot over time.

And now China is really the big engine there, and the big country. And a lot of the countries in emerging markets, going back 20 years ago, that were benefiting from a weaker dollar because they borrowed a lot in US dollar. And so as the US dollar would come down, paying it back was easier.

A lot of those countries, some are not even in the emerging markets benchmark anymore. So I think that's a little bit of a shift in terms of how we should think about the tailwinds of a weakening US dollar.

HEATHER: OK. All right. Well, that's helpful to think about that shift. One of the big headlines coming out of Europe, Yasmin, has been the large fiscal stimulus plans happening in countries, like Germany. Of course, home to the EU's largest economy.

What is the reasoning for all of this extra spending that we're seeing overseas? And could that pay off in the future?

YASMIN: I mean, Trump has always advocated that Europe, in particular, but Japan as well, and other countries, pay more of their fair share in military. And the US has been a military backstop. They've been there for a lot of the allies.

And I think this time through, in talking to a lot of business leaders, folks abroad, there's a sense that, this time, Europe, Japan, they need to increase their spending. And they're savvy in terms of their own defense, and take these capabilities seriously, and take the reins back.

And so that's the beginning of the catalyst. However, some of the fiscal spending, which is geared toward defense spending, is also spilling into places like infrastructure. And this is going to, generally speaking, when you have these big packages—and this is \$1 trillion for the next 10 years out of Germany—it tends to spill over into other areas of the economy.

And that's what we would expect to happen, whether it's the banks, the companies that are helping with the infrastructure projects. And if other countries also step up and start to spend, you'll see that even larger.

In Japan, you're having a similar situation, where the spending is increasing for defense. So I think this is truly taking hold. And I believe that the policies outside of fiscal stimulus policies will also shift to allow for companies to be competitive with US companies.

HEATHER: You mentioned—

JURRIEN: I would just—

HEATHER: Oh, go ahead. Go ahead, Jurrien.

JURRIEN: No, I would just add to that. What we're seeing in the US, of course, is a shift. At the beginning of the year, it was about cutting spending. And now the emphasis out of Treasury especially is, we can't really cut spending, so we're going to outgrow the debt. And that's what the Big Beautiful Bill is. And maybe an AI productivity boom.

And I think maybe that that sentiment is spreading to other parts of the world, where austerity, like we saw with Greece in the sovereign debt crisis many years ago, it doesn't always work. And I think there is a sense now that, OK, let's spend more, even though it's going to create more deficit.

But growing faster when you have this big debt burden, and this aging population, is something that I think is spreading around the world. And I think that's what Yasmin is referring to here.

HEATHER: Try to outgrow the spending when you can't cut the debt. All right. You had mentioned Japan, Yasmin. We talked about those trade agreements at the top of the show, with the EU and with China.

But also last wee, important to remember, the administration did reach a tariff deal with Japan. So I'm curious what your thoughts are on Japan, and what the potential is in that space?

YASMIN: I mean, I think the tariff story has been a big cloud over Japan. And getting some clarity on the level is really helpful, even if it is going to be at a level that is quite difficult for some industries.

I think that the Japanese landscape is undergoing pretty significant transformation, making it compelling for investing. The country is experiencing a virtuous cycle of wage growth, proactive price setting by corporations, and a shift in longer term inflation expectations, after a long period of deflation. So a little bit is actually pretty good.

And then there's key drivers that hinge more on corporate governance. In Japan, there's been a big push for companies to improve their competitiveness with other Global Champions, and really focus on profitability metrics.

This means restructuring their businesses to achieve growth, and enhance that profitability. So we're seeing this play out in a number of areas, some of the big conglomerates that have gotten out of underperforming businesses, and really looking at where there's a structural growth opportunity.

So that's what we get more excited about. And then, interestingly, sometimes there's a silver lining in the aging demographics, which is typically thought of as negative. But you have natural attrition.

So, oftentimes, Japanese companies that needed to rightsize couldn't due to labor laws. And now you have the aging population, the natural attrition that I mentioned. And you make up for productivity through technology gains. And that's been exciting to see as well.

HEATHER: OK. Well, hey, Jurrien, one of the biggest drawbacks perhaps, or one of the biggest draws, rather, to international stocks draws, has been the price. Because of course, everybody loves a bargain.

And right now, it does seem like you can get a lot more for your money overseas. But could there be a drawback here? Is there a potential that this could be a value trap, because it had been a cheaper market for so long, Jurrien? Or do you think the catalyst and the current dynamics are enough to drive improvements in international earnings? What's your thoughts on this, Jurrien?

JURRIEN: I think that the value trap argument certainly existed maybe a decade ago. In Japan, you had zombie companies. And in Europe, you had these banks burdened with all of this bad debt, they still back the eurozone debt crisis.

But that's all been cleaned up. Japanese companies, as Yasmin said, are much more shareholder friendly now. And it's interesting that when you look at, in my view, are the two drivers of valuation.

So the US is obviously more expensive than the rest of the world. But for good reason. Because it's growthier. It's earnings growth is higher, or has been higher. And more of that earnings have been paid out to investors in the form of dividends and share buybacks.

But Europe and Japan have really caught up their payout ratio, which is what that's referring to, are really quite competitive with the US now, even though the earnings growth rate is still behind. But maybe that will change.

So I definitely would not consider it a value trap anymore. There are definitely reasons to consider international markets. There might be less of a capital gain feature, and more of a yield feature, like a dividend yield feature. But it's a good diversification strategy. And especially if the dollar continues to edge lower here, you get that currency translation that Yasmin was talking about earlier as well.

HEATHER: All right. Not a value trap in your mind. We are pretty much at time, Yasmin. But quickly. I'd love to talk about the future. What are the reasons the US market has been so strong, is our technology sector is so much stronger than non-technology sectors in the US.

With all the innovations in AI, it makes sense that these US companies are doing so well. But are there any markets outside of the US where you see they have the potential to lead the AI space going forward?

YASMIN: Yeah, definitely. So I think we all think of artificial intelligence as the biggest trend that's happening right now in our world. And we think of it often as a US phenomenon, where a lot of the large language models that we use are coming out of the US. They were born out of the US. And a lot of innovations going on.

And I'm going to name some stocks probably, but they're not recommendations. They're just things to bring attention to the global scope of AI.

Probably a lot of us know Taiwan Semiconductor Manufacturing, TSMC. It's the only manufacturer of the most cutting-edge chips out of NVIDIA. The machines that make these are made by ASML out of the Netherlands.

This is very, very global. The other thing that I'm pretty excited about is the build-out in cloud, which is necessary. The compute that you get from hyperscaler build-outs across the globe in order to fuel artificial intelligence.

The European build-out, the Japanese build out is a little bit behind. You have different data, policy, laws. But it's coming, and it's ramping, and innovation is happening. So I think this is another area that is not just excitement in the US, but it's also in other markets.

HEATHER: All right. Thank you for disclosing. Not your stock recommendations.

YASMIN: Correct.

HEATHER: The dominant position in non-US markets. Just a few names. Jurrien, we're right at time right now. But of course, we always have to wrap with a Timmer's Take, and talk about what you're watching for the week.

Of course, the Fed meeting today and tomorrow. When the Fed has that press conference tomorrow afternoon, what are you going to be watching for?

JURRIEN: So, obviously, there's earnings season. 200 companies reported. That's going very well. What will happen with the Fed this week? Not so much whether they cut rates, because they're not expected to. No one really is expecting them to.

But to see whether there are dissensions with the non-rate cut, if that's what ends up happening. That'll be an interesting political development, because it might set the stage for how the future of the Fed, what that's going to look like, with Powell retiring from the chairmanship role next year. And then members who are clearly advocating for their replacement. We'll see whether they make some noise this week or not.

HEATHER: And that's something we're going to be watching alongside you, Jurrien. And we'll be talking about it on next week's *Market Sense*. But we do have to leave it at that for today.

If Yasmin and Jurrien have you thinking about doing a little more research on the international stock space, just wanted to let you can bookmark [Fidelity.com/InternationalInvesting](https://www.fidelity.com/InternationalInvesting).

And then once today's replay is posted to our *Market Sense* page, we'll also provide a link to a great article from our Viewpoints team on some international ETFs you might want to consider.

You'll just want to click on the link right underneath our video player, on [Fidelity.com/MarketSense](https://www.fidelity.com/MarketSense). That's our homepage, [Fidelity.com/MarketSense](https://www.fidelity.com/MarketSense).

On behalf of Jurrien Timmer and Yasmin Landy, I'm Heather Hegedus. Terrific job, guys. And remember, we're on live Tuesdays at 2:00 Eastern. Hope to catch you next week. Bye.

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