Monthly Update | Issue 100 | 15 May 2025

Rising markets, restless waters: outlook for a volatile recovery

Key takeaways

- Several positive developments have been taking place during the last few weeks. The US reached a trade deal with the UK and agreed to trade talks with China, held last weekend in Geneva. Recent US macroeconomic data are mixed but remain in expansion territory. Companies have posted better-than-expected earnings.
- While earnings growth is forecasted to slow in the quarters ahead, we expect lower interest rates and pro-growth policies, such as deregulation and tax cuts, to help support the economy.
- Further easing of trade tensions could improve sentiment among consumers, businesses and investors. However, reaching trade deals with countries where the US runs sizable trade deficits may prove more challenging.
- The peak in trade uncertainty and market volatility may be behind us, but history shows that bottoming is a process. Markets could remain rangebound for a time, with periodic bouts of volatility, before working back toward early-2025 highs.
- Stay invested. Trying to time the market is a dangerous game. Our equity market allocation is neutral versus our strategic asset allocation (SAA), which is roughly 47% of equities allocated to global equities within a balanced account.
- Keep some international diversification, but beware, US exceptionalism is NOT dead. Many of the world's strongest companies are listed in the US and tariffs/weaker USD are negatively impacting other regions like Europe.
- Focus on quality, style/sector and asset classes diversification
- We keep our gold and hedge funds exposure for diversification purposes. Our stance on currency (positive euro vs the US dollar, neutral dollar against other major pairs) is unchanged.

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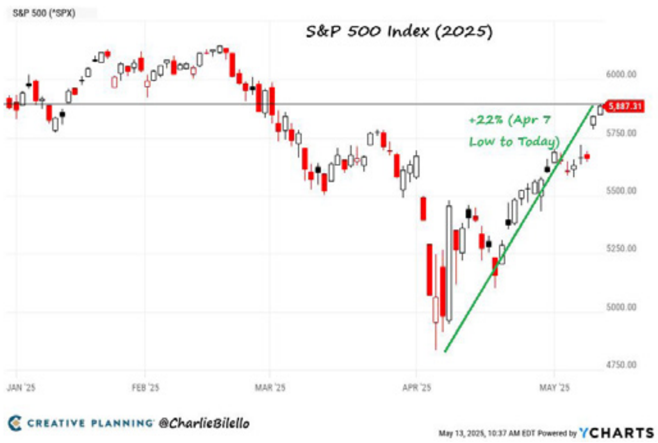
Global financial markets experienced significant volatility during the month of April, largely driven by US trade policy shifts, particularly President Trump's tariff announcements.

Indeed, markets were rocked by Trump's "Liberation Day" tariff announcement on 2 April, imposing a blanket 10% tax on imports, with higher rates on specific trading partners, escalating to 145% on Chinese imports. This triggered a sharp sell-off, with the Dow Jones Industrial Average dropping 2,200 points and the S&P 500 falling 6% in the worst week since 2020 with global equities losing over $5 trillion in market value. The stress was also visible in the US Treasury market which experienced rising bond yields despite the equity sell-off—a rare event—and in the forex market as the dollar suffered one of its biggest sell-off in recent history. Gold surged as global investors decided to look for shelters in time of heightened uncertainties.

However, to the surprise of many, main equity indices managed to recover all their losses since, as the S&P 500 and the Nasdaq are now back into bull market territory (defined as a 20% rise from recent lows). Meanwhile, the bond market and the dollar have both been stabilising.



Source: Bloomberg

So, what are the key factors behind this V-shape rebound?

- Easing tariff concerns: a US-China agreement announced on 12 May to temporarily reduce tariffs alleviated fears of a global trade war, prompting a broad market rally. The constructive tone of trade talks in Geneva between US officials and China further supported optimism.
- Strong earnings: robust Q1 earnings from companies like Microsoft and Meta Platforms exceeded expectations, boosting investor confidence, particularly in the tech sector.
- Economic data: a lower-than-expected Consumer Price Index (CPI) report on 14 May showed annual inflation at 2.3%, the lowest in four years, easing concerns about tariff-driven inflation.
- Federal Reserve policy: the Fed maintained interest rates at 4.25%-4.5% in May, signalling caution but supporting market stability with no immediate rate hikes.
- Market liquidity: the Federal Reserve provided $3.5 billion in liquidity to Wall Street banks on 7 April 7, coinciding with the Nasdaq's yearly low, which supported a strong rebound in equity markets
- Market sentiment and technicals: investor sentiment shifted from extreme pessimism to neutral, with the Fear & Greed Index rising from 44 points to 48 by 1 May. Market breadth improved, with 44.4% of S&P 500 stocks and 29.8% of Nasdaq stocks trading above their 200-day moving averages by 9 May, indicating broader participation in the rally.
- Technical signals, such as the S&P 500's rare thrust signal on 25 April and the Nasdaq's break above its 200-day moving average, supported bullish momentum.

So, what's next? Are global equity markets going to resume their long-term bull market? Is it time to overweight US equities again? Or should investors stay cautious instead of jumping into the bandwagon?

An unusually broad range of potential macro scenarios

The new US-China deal to temporarily cut tariffs is better than expected, providing near-term relief for investors. Under the deal, so-called reciprocal tariffs will drop from over 100% to 10% on both sides. The Trump administration will keep 20% fentanyl-related tariffs on China in place, meaning America's total duties on Chinese imports will stand at 30% while the 90-day pause is effective.

While the deal unveiled in Geneva was better than anticipated, uncertainty remains as it would be difficult for Beijing and Washington to reach a more concrete trade arrangement in just three months. However, it keeps the pressure on the negotiation process, which is good. We are still waiting for further details on other terms of this agreement, for example, if China would relax on rare earth export restrictions.

As such, we continue to believe that the global economy is currently facing an unusually broad range of economic scenarios. Below we outline three possible outcomes with an estimated probability assigned to each of them. The main scenario could potentially lead to range-bound markets. The pessimistic scenario could lead to more downside. The optimistic scenario would bring us to new all-time highs for equity markets in the coming months. Stay tuned.

	Main scenario (probability: 55%)	Pessimistic scenario (probability: 25%)	Optimistic scenario (probability: 20%)
Geopolitics	• Tariffs with most major economies stabilize around 20%, with limited retaliations • The "Tit-for-tat" with China remains but gradually de-escalates • Ukraine-Russia: no lasting ceasefire	• The full trade war cannot be avoided as Trump sticks to his ideologic view while China refuses to fold • Countries are forced to choose between the US and China • Global trade decline	• Trump agrees on a Trade deal with at least Europe & Japan + some pedaling back on China • Ukraine and Russia agree on the terms of a peace deal • Global Trade resumes after recent turmoil
Inflation & policy mix	• Despite stagflation risk, the Fed cuts rates 3 times. US implement moderate tax and spending cuts • Europe & China ease monetary policy as well • China expands fiscal boost	• A liquidity crisis forces central banks to cut rates despite high inflation • High fiscal deficits increase long term premia and funding costs	• Outlook on inflation becomes clearer, enabling the Fed and other central banks to cut rates several times in H2 • Financial conditions ease • Fiscal policies boost growth
Global Growth	• The US barely avoids recession • Global growth is hurt by tariffs, delaying return to potential growth • EM grow faster than developed markets	• Business leaders and consumers' confidence tumble. • Bankruptcies and corporate default rate increase • A global recession cannot be avoided.	• Protectionism tensions subside • Deregulation, lower taxes and AI productivity boost growth • Global economy grows above trend

Source: Bloomberg

In parallel, while economic activity remains subdued in Europe and China, recent developments have been rather reassuring. Both regions have stabilised since last year's pronounced deterioration. In China, after a first plan in September to stem the collapse of the real estate market, revive credit growth and support the equity market, the authorities are set to continue supporting economic activity this year, with a much-awaited plan targeted toward domestic consumption. In Europe, a potential shift to more growth-supportive policies will, even in a best-case scenario, take time to materialise, and remains subject to elevated uncertainties. Furthermore, the prospect of US tariffs remains a significant headwind for sentiment and activity in the short run. However, the continuation of monetary policy easing by the ECB, the SNB and the BoE are likely be supportive for economic activity and to contain immediate downside risks to growth.

THE WEIGHT OF THE EVIDENCE

Our asset allocation preferences are based on 5 indicators, including 4 macro and fundamental indicators (leading) and 1 market dynamics (coincident). The weight of the evidence suggests maintaining a constructive view on equities (neutral). Below we review the positive and negative factors for each of them.

Pillar 1

Macro cycle (NEUTRAL)

Global growth is facing headwinds from the US tariff announcements made on 2 April, which have already had some impact on trade and have fuelled fears of inflation in the US. The suspension and rollback of tariffs, including the most recent announcements with China, provides hopes that the short-term impact could eventually be contained and that the medium-term impacts might end up being limited. However, uncertainty has not been (yet?) fully dispelled and the blow to confidence might take some time to dissipate. While risks of pronounced growth slowdown in Q2 remain, particularly in the US, China and Germany, resilient labour markets, prospects of trade tensions' easing and more supportive monetary and fiscal policies ahead are helping to cushion the impact.

US: The job market remains strong, supporting consumer spending despite tariff-driven inflation concerns. However, sentiment is weakening, and risks remain tilted to the downside if trade tensions persist.

Eurozone: Early signs of recovery, especially in Southern Europe and Germany, are now threatened by US tariffs and potential overcapacity from China. Inflation pressures are easing, and the ECB is set to continue rate cuts.

China: Stimulus measures have improved sentiment and activity, but weak domestic demand and the export hit from tariffs continue to weigh on growth.

The macroeconomic environment is currently rated neutral for risk assets. Positive fundamentals such as robust labour markets and accommodative monetary policy are offset by uncertainties around trade policies and inflation uncertainty.

Pillar 2

Liquidity (POSITIVE, based on forward-looking factors)

Tax collection in April has withdrawn some liquidity in the US but the upward dynamic is expected to resume in May, especially as no agreement on the debt ceiling is in sight (TGA will decline again in the coming weeks). Rising M2 liquidity and US dollar weakness support global liquidity.

The liquidity backdrop is positive for risk assets with prospects of monetary policy easing, fiscal support, liquidity injections and a weaker USD pointing to supportive liquidity dynamics in the months ahead.

Pillar 3

Earnings (NEUTRAL, upgraded from negative)

90% of the S&P 500 have reported Q1 earnings: 78% of them are beating estimates and the blended growth rate is 13,4% YoY.

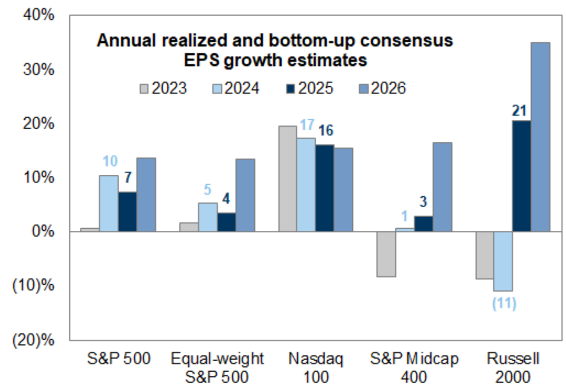
The expected earnings growth for the main US equity indices remains quite constructive for 2025 and 2026.

It is also interesting to note that the vast majority of S&P 500 companies guidance remains unchanged, which is a surprise as many analysts were expecting rather gloomy outlook by executives.

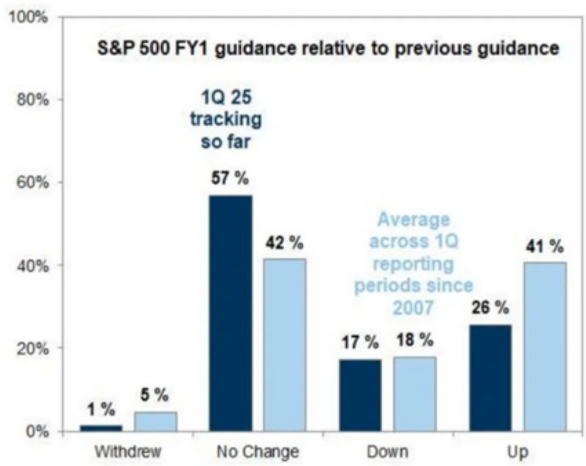
However, we note that downward revisions have been more aggressive in the rest of the world than in the US as currency appreciation is a headwind for companies in Europe and in Asia.

Earnings growth

Exhibit 34: Realized and consensus EPS growth for select US equity indices



Source: FactSet, Goldman Sachs Global Investment Research



Source: FactSet, Goldman Sachs Global Investment Research

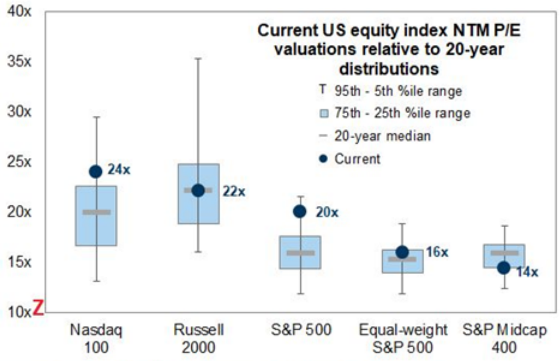
Pillar 4

Valuations (NEUTRAL)

Valuations also improved in April and already shifted from negative to neutral a few weeks ago. The recent rebound in equity markets has been driven primarily by multiple expansion rather than fundamental earnings growth, raising some concerns about the sustainability of the rally. US large-cap stocks continue to trade at a premium relative to historical levels, but the broader market—including smaller-cap and international equities—now trades at or below long-term median valuation multiples. This normalisation suggests a more balanced risk-reward profile for diversified investors, assuming earnings don't deteriorate further in the coming quarters.

We note that Warren Buffett's favourite valuation tool— the market cap-to-GDP—shows that the S&P 500 recently traded around 168% market cap-to-GDP vs the global equity markets at around 90%. That suggests US stocks are (still) expensive relative to the rest of the world.

US Equity index P/E valuations vs. history

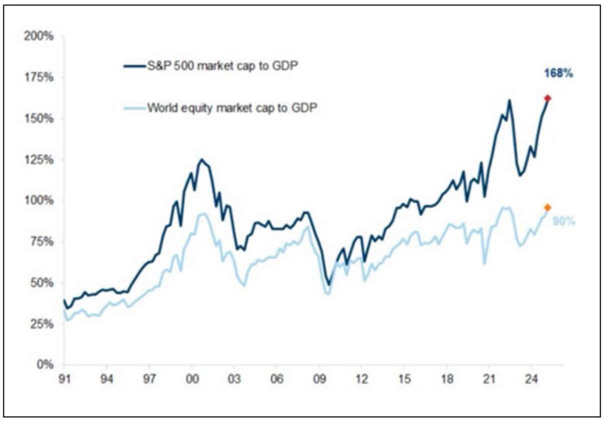


Pillar 5

Market Factors (from POSITIVE to NEUTRAL)

The aggregate market factors' signal has increased from 75% to 100%, reflecting a stronger positive outlook across key metrics. This shift is based on notable improvements in market sentiment, technicals, and trend indicators over the past week.

The current regional scores (USA at 75% and Europe at 90%) both exceed the threshold of 75%, supporting the move to a fully positive stance. This allocation reflects increased confidence in both regions' near-term performance.



Indicators review summary - our five pillars

Earnings has been upgraded to neutral. Market factors have been upgraded to positive.

With 2 pillars (liquidity and market factors) signalling an overweight and 3 in neutral (macro, earnings and valuations), the weight of evidence is neutral for equities.

Underweight -	Neutral =	Overweight +
	Macro Cycle	
		Liquidity
➔	Earnings Growth	
	Valuations	
	➔	Market Factors

INVESTMENT CONCLUSIONS

- The peak in trade uncertainty and market volatility may be behind us but history shows that bottoming is a process. Markets could remain rangebound for a time, with periodic bouts of volatility, before working back toward early-2025 highs.
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TACTICAL ASSET ALLOCATION (TAA) DECISIONS

Positive market effects have pushed the equity allocation back to neutral in the TAA grids

Asset Allocation Grid

TACTICAL ASSET ALLOCATION (TAA) 8.05.2025

	Underweight -	Neutral =	Overweight +
Asset Classes		Cash	
		Equities	
		Fixed Income	
		Alternatives	
Fixed Income			Govies 1-10 (local)
	Govies 10+ (EUR)	Govies 10+ (USD, CHF, GBP)	
		Corporate IG (local)	
		High Yield (local / global hdg)	
		EM Debt	
Equity		United States	
		Eurozone	
		UK	
		Switzerland	
		Japan	
		Emerging Markets	
Alternatives		Hedge Funds	
Commodities			Gold
		Commodities	
Forex (vs. USD)			EUR
		CHF	
		GBP	
		JPY	
		EM Currencies	

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