Uncertainty May Provide Opportunity

MAY 2025

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What's happened? *Downside macro risks are rising*

The aggressive imposition of tariffs by the United States has ratcheted up already rising geopolitical concerns. The consequence has been a dramatic shift not only in growth and inflation expectations but also of fiscal policies and, potentially, eroding trust in US assets, leading to a retreat of foreign capital, as evidenced by the large downward move in the US dollar.

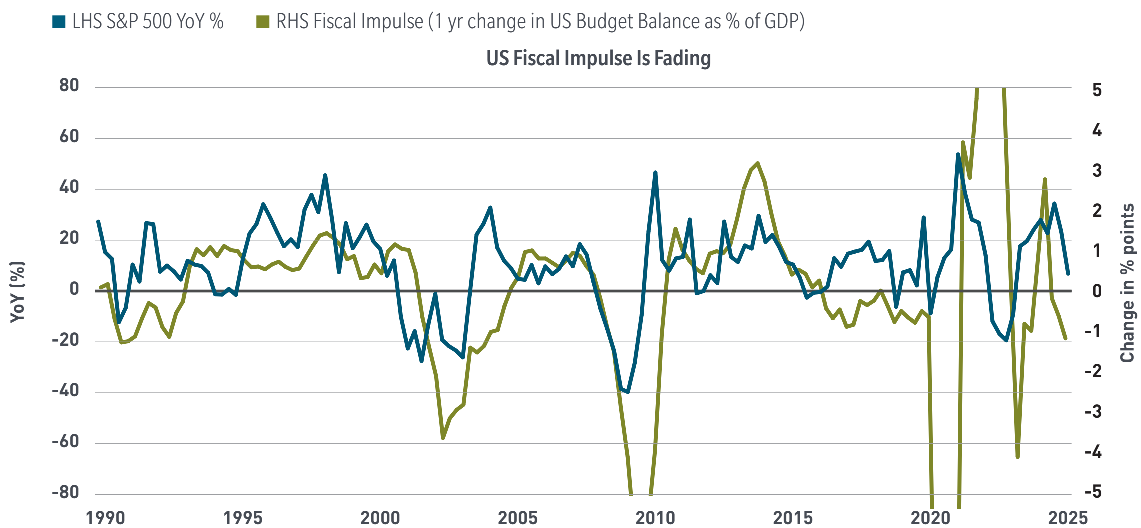
Inflation impacts may well prove to be transitory; the impact on global growth may be of the greatest concern. Sentiment indicators are decidedly negative, and near-term data may continue to be influenced by businesses and consumers seeking to get ahead of the tariffs.

Consumers are likely to be impacted in several ways, and this could lead to a change in their behavior.

Factors bringing about this change could include poor sentiment possibly leading to higher savings and lower consumption and fear of job losses due to reduced global trade and slowing corporate profits. There is also the potential backlash against brands in the face of growing anger over the US administration's approach. There is already evidence of fewer foreign tourists visiting the US.

While the data show no significant signs of economic weakness just yet, the next few months will be crucial. In addition to tariffs, the US is tightening its fiscal policy as the administration aims to reduce the deficit. Cutting government spending is positive for the financial health of the US in the long term but will have negative short-term consequences for the economy.

Exhibit 1: US can no longer rely on fiscal spending to drive growth



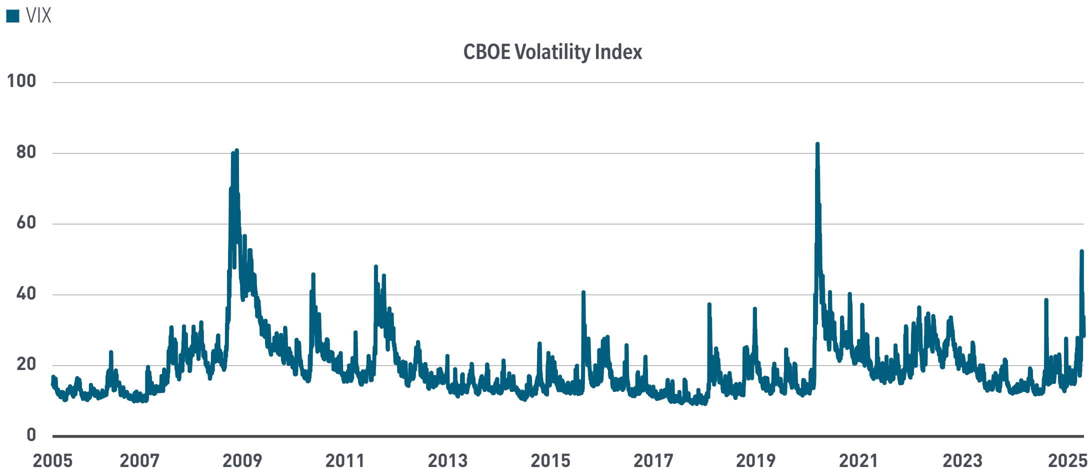
Source: Bloomberg. Quarterly data from 31 December 1989 to 31 March 2025.

Why is it important? *Expect greater market volatility*

Transitions create friction, and in this environment we expect volatility to remain elevated. Equity markets may react more to announcements than data in the near term as analysts attempt to recalibrate their expectations of corporate earnings in a constantly changing macro and policy environment. As a major importer, the US is facing supply disruptions far more complex and difficult to address than a fall in domestic demand.

We feel we know the cause and the cure. Normally, volatility is driven by market events and policymakers come together to fix the issues. While there may be uncertainty as to whether the policies will work as desired, they are typically pulling in the same direction. In this case, it is the policies and the lack of transparency as to the goals that are driving the volatility. This could be corrected, but we don't know whether or when, and unsurprisingly, traditional relationships are breaking down, such as the US dollar and Treasury weakness in a risk-off environment.

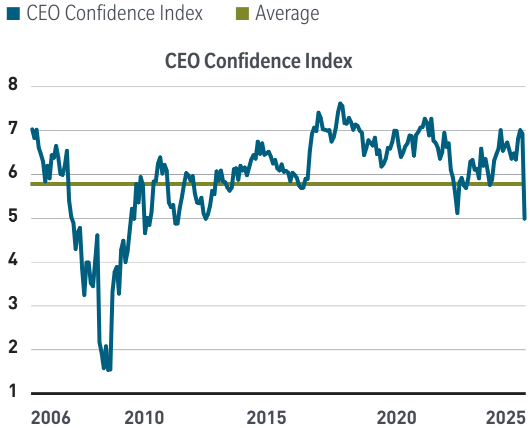
Exhibit 2: Equity market volatility significantly elevated

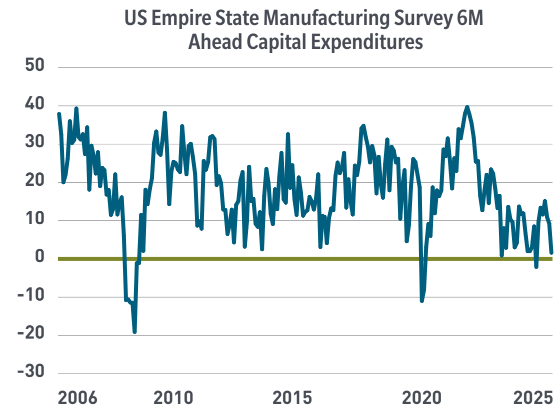


Source: Bloomberg Daily Data 17 April 2005 through 17 April 2025.

Corporate earnings face a headwind as economic growth looks set to slow due to tariffs and trade restrictions. We have yet to see where the tariffs land, what comes of reciprocal negotiations and how other countries retaliate; all of this creates an uncertain environment in which companies must make long-term capex decisions. Commitments may or may not turn into investments until there is policy clarity, and it will take years to deliver on and see the return from projects. Additionally, this should drive higher working capital requirements, which negatively impact margins.

Exhibit 3: Sharp drop in US business confidence and capital spending



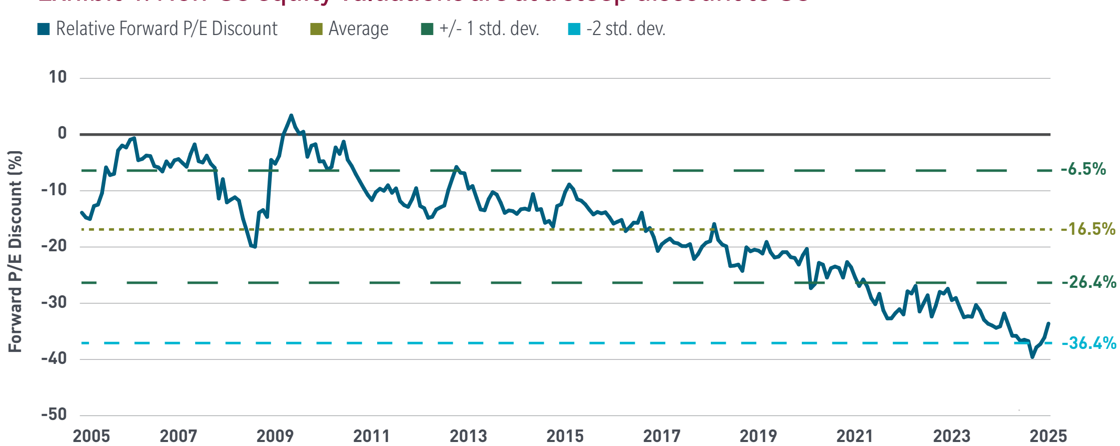


Source: FactSet Market Aggregates. Monthly data as of 31 March 2005 to 31 March 2025. Forward = next-twelve-months estimates. US = S&P 500. Non-US Equity = MSCI ACWI ex USA. LHS – Forward P/E Discount = MSCI ACWI ex USA Forward P/E divided by S&P 500 Forward P/E minus.

How does it impact investors? *Know what you own*

Starting points matter, so it's worth looking beyond the US. US equities have been trading at historically elevated valuations while global multiples remain in line with or at a discount to their longer-term averages. As the US embarks on fiscal tightening at the same time as fiscal expansion in Europe and China, it merits considering non-US equity allocations to diversify portfolios and seeking a greater margin of safety.

Exhibit 4: Non-US equity valuations are at a steep discount to US



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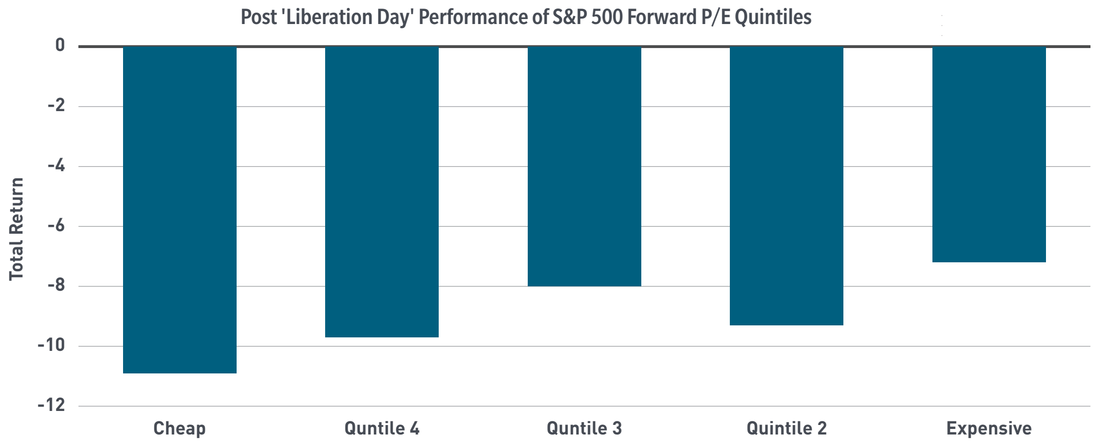
In this environment, investors need to seek out resilient companies that can navigate uncertainty. Valuations, the driver of cash flows and risks to cash flows, take on increased importance. All of this leads to increased dispersion across sectors and regions, which should be beneficial for active managers as they seek to find winners and avoid losers. Broad indices may be overexposed to companies and regions more at risk.

Exhibit 5: Valuation not value — cheapness is not necessarily helping



Source: FactSet Portfolio Analysis. Daily data from 2 April 2025 to 21 April 2025. Stocks are ranked high to low based on their forward P/E daily and quintiles are constructed using an equal-weight methodology. Forward = next twelve-months. Cheap = Quintile 5. Expensive = Quintile 1.

Be selective. We continue to prefer non-US over the US due to relative valuations and differences in policy. We believe the current backdrop is supportive of alpha over beta. While some sectors, regions or factors face stronger headwinds, companies, even those doing similar things, could be impacted differently based on their manufacturing base, supply chains and location. Those that provide critical non-substitutable products and have pricing power are well positioned.

Past winners may not be future winners. Fortunes may change as the level of disruption to global trading and financial systems drives structural shifts. We continue to believe a defensive posture is appropriate and see the following as providing attractive opportunities; however, selectivity remains key:

- Within non-US, Europe and Japan > Emerging Markets
- Value > Growth
- Large caps > Small caps
- Low beta > High beta

SUMMARY: OPPORTUNITIES IN UNCERTAINTY

Market selloffs provide opportunities for patient investors with the ability to tune out the noise and focus on what matters for a company to survive and potentially thrive from not only the current turmoil but its ability to adapt to the structural changes this brings.

These are not normal times; with downside risks to growth and earnings, investors should be focused on resilient compounders with high-quality assets at reasonable valuations.

The impact of tariffs will be company-specific and depend on how supply chains are structured. In these times, it's crucial to know what you own.