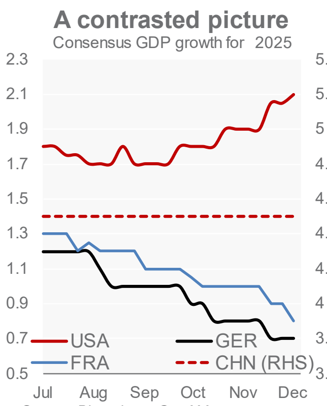
OUTLOOK 2025

Trumponometer

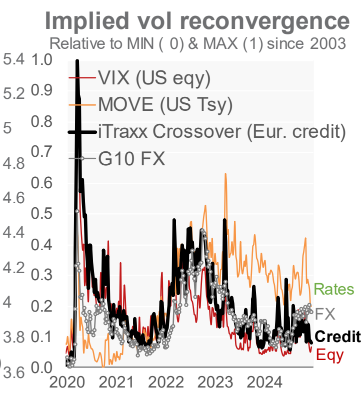
December 13, 2024

Our Annual Outlook provides our key views and investment implications for the coming year

- **The return of President Trump implies a higher level of policy uncertainty, making the traditional year-ahead outlook an even more difficult exercise. Our core assumption is that Republicans cannot afford another inflation shock into the mid-term election, hence will prioritise policies rather than embracing full-on Trumponomics.**
- **Global growth is set to stabilise at cruise speed in 2025, with marked regional differences, e.g. 3 times faster in the US than the Euro Area. The desynchronisation of the growth cycle is set to feed into the inflation one: we see risks balanced in the EA but skewed to the upside in the US.**
- **Greater policy uncertainty, selected ambitious valuations (SPX, USD), and concentration all point towards a rise in financial volatility in 2025. This has started already in the FX space; next credit and equity. Instead, we see room for rates volatility to normalise further, though inflation uncertainty will keep it above the pre-Covid lows.**
- **Our directional views are constructive for 2025. We embrace a small long duration in EUR but wait for a better entry in the US (10-year UST > 4.50%). Our structural long in Credit remains, even at these tight levels. In a challenging year for EM markets, our preference goes to Hard Currency debt. We expect single-digit equity returns in 2025 and run a moderate overweight; cheap implied volatility offers hedging opportunities. We expect further (moderate) USD gains, with risk on both sides. A transactional Trump would push the dollar lower, while "full-on" Trumponomics would push it much higher, at the risk of derailing global growth and financial stability.**



Source: Bloomberg, GenAM



Source: Bloomberg, CBOE, JPM, GenAM calc.

CONTENT

TRUMPONOMETER

Vincent Chaigneau

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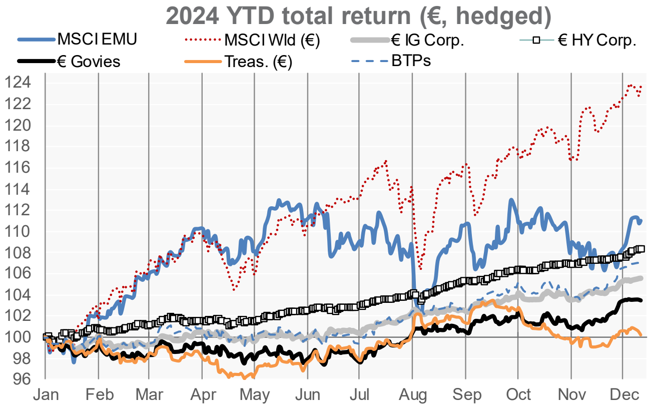
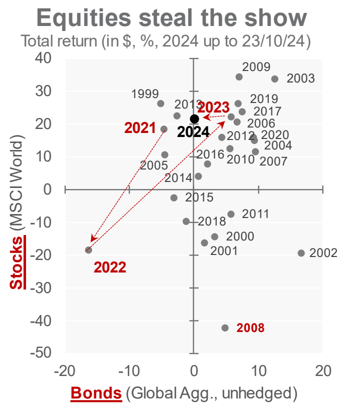
2024 another great year for US equities; mixed for rates, yet again good for global credit and the US dollar

The US equity market, and the rest. The strong performance of global balanced funds over the past 15 months, and even 27, owes to unstoppable US equities. The left chart below shows 2024 returns, up to 12/12. The MSCI World (nearly 75% US) has delivered a 23% return in EUR (hedged). At the bottom, US Treasuries are flattish, as the Trump trade pushed long yields above end-2023 levels. Still, 2024 returns have vindicated our positive tone a year ago ("2024 Outlook – The intangible cycle"). The second chart indicates a mediocre year for Fixed Income (Global Aggregate flattish), but this is in USD, unhedged: dollar gains have eaten into non-USD FI gains. For EUR investors, rates and credit have delivered solid returns, more so in riskier segments (AT1, High Yield). We expect a decent year in 2025, but a more volatile one, that will largely depend on the US policy stance: measured or full-on Trumponomics?



Source: Bloomberg, GenAM calculations



Source:Bloomberg, GenAM

Source: MSCI, Bloomberg, GenAM calculations

Consensus is rather sanguine again

So was it a year ago, and this eventually did not prevent a solid year for asset prices. Yet the consensus often gets punished, and it remains to be seen when the

Consensus priced for stable growth, moderate disinflation but ongoing rate cuts

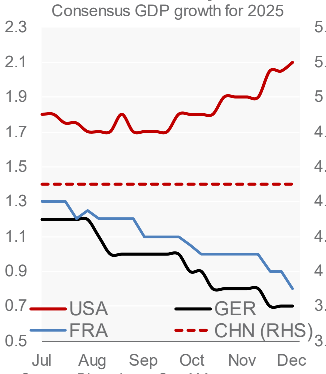
nearly perfect economic landing assumed in asset prices will be realised. The consensus sees world GDP growth about stable at 3.1%, some further (but not full) inflation normalisation (global CPI from 4.5% in 2024 to 3.5% in 2025, i.e. the lowest since 2020) as well as ongoing central bank rate cuts (Fed at least 50bp, ECB 100-125bp etc.) – see charts below.

Inflation risks skewed to the upside in the US, but balanced in EUR

Desynchronisation. Our own rate cut forecasts are slightly bolder than market implied. The first chart below shows a very contrasted growth picture at the regional level. The US economic dominance will persist under Trump, and our US growth forecast (2.4%) is above the street's median. Instead, we expect Euro Area growth to stabilise at 0.8%, below the 1.1% consensus. We agree that a bolder Chinese stimulus will put a floor on China growth (4.5% next year), though the outcome there will partly depend on the global trade tensions. The latter, as well as the widening gaps in technological progress, have contributed to some desynchronisation in the growth cycle. This may now feed into some desynchronisation of the inflation cycle. We see US inflation risks skewed to the upside (tight output gap, Trump policies), but those in EUR much more balanced – not least because China's overcapacity problem may grow on tariffs, which may see the country export its deflation pressure.

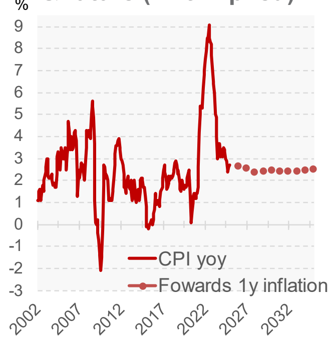
A contrasted picture

Consensus GDP growth for 2025



Source: Bloomberg, GenAM

US inflation, past, present & future (mkt implied)



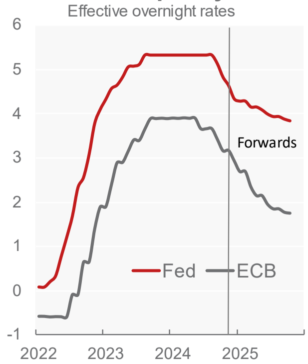
Source: Bloomberg, GenAM calculations

€ inflation, past, present & future (mkt implied)

Source: Bloomberg, GenAculations

USD & EUR policy rates

Effective overnight rates



Source: Bloomberg, GenAM

'Trumponometer': measuring Trumponomics

Shall we position for a divisive or a deal-making Trump? This matters for investors

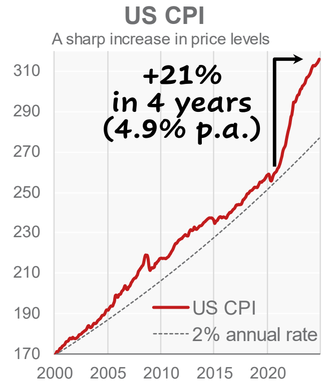
President Trump cannot afford another inflation shock. "Prediction is very difficult, especially if it's about the future!" It always is, but maybe more so into a year that will mark the return of President Trump. Tweets (Xs) will cause daily volatility along the way, but it is the direction of travel that will matter: shall we position for Trump to be the divisive self, or the deal maker? The answer may have a considerable impact on global markets.

Republicans will be wary of causing another inflationary shock that would surely ruin their chance at the mid-term elections in just two years

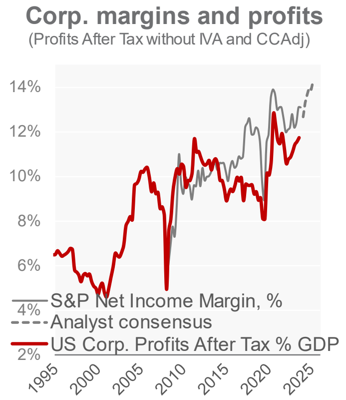
Trump's policy pillars include 1/ Deregulation; 2/ Tax cuts; 3/ Immigration cuts; 4/ Tariffs. Those policies – except maybe the first one (positive supply shock, but potentially boosting demand too) – are largely inflationary (respectively a positive demand shock and negative supply shocks). We argue that the inflation shock, and elevated prices, have largely contributed to the poor electoral performance of incumbent governments in 2024 (from the US to the UK, France and even Japan). US consumer prices are up 21% over the past 4 years, making a mockery of the Fed's target. Inequality may be another cause of voters' unhappiness, and the secular rise of profits as a share of GDP (second chart below) has contributed to the widening gap between those who own capital, and those who do not. Trump's policies will not address inequality. But Republicans will be wary of causing another inflationary shock that would surely ruin their chance at the mid-term elections, in just two years.

We expect a solid delivery on deregulation and tax cuts, but a more measured approach on tariffs, immigration and the fiscal impulse

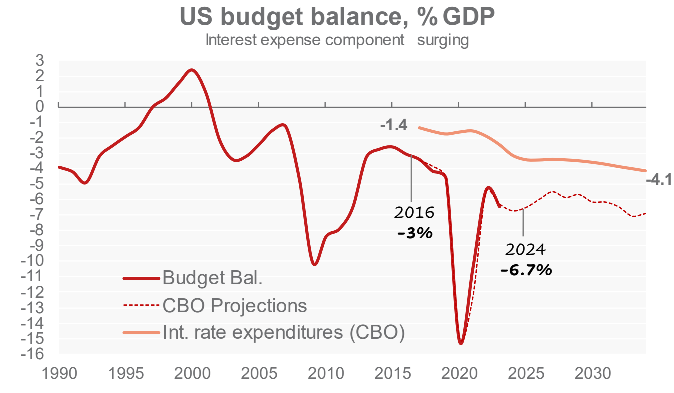
Hence, we expect Trump to prioritise policy actions: we assume a strong delivery on deregulation (energy, banking etc.) and tax cuts (we assume the corporate tax rate to be cut from 21% to 17-18%). On tariffs, no doubt the stance towards China will be tough, but more generally we assume a transactional approach where tariffs are used as a platform to negotiate better trade deals. Likewise, we expect a more measured approach on immigration, whereby the massive inflows under the Biden administration will be reduced (this has started already) but not reversed. We assume a very limited fiscal impulse, with tax cuts being partly offset by spending cuts. The budget deficit is more than double where it was when President Trump started his first mandate (right-hand chart below), which will limit the Congress' appetite for further fiscal expansion.



Source: BLS, Bloomberg, GenAM



Source: US BEA, BBG, GenAM

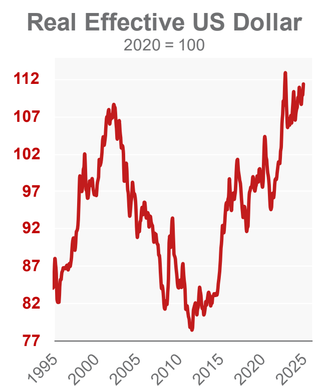


Source: CBO, Bloomberg, GenAM

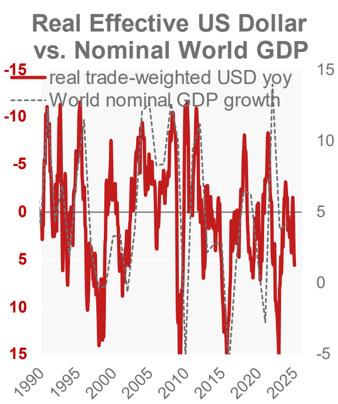
A more volatile financial year ahead

Policy uncertainty and USD position crowding make the all-important USD view more difficult

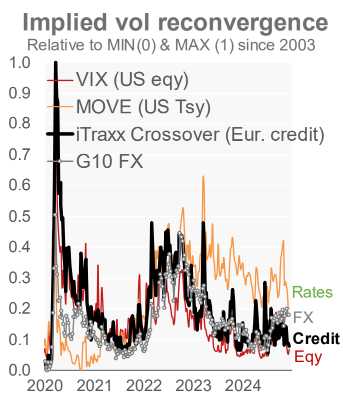
Trumponomics and the US dollar. The US policy stance will matter for all markets, but none more than FX maybe. The US dollar troughed in the aftermath of the Great Financial Crisis, in summer 2011. Since that, it has gained more than 40% on a trade-weighted, inflation-adjusted basis. Half of those gains have occurred in the past four years. This has made the US dollar rich on a fundamental basis. We expect moderate further strength in the policy context describe above. But there is ample room for policy surprises. Also, the bullish dollar view is consensual and crowded, which implies a greater risk of correction. Should President Trump push his policy levers aggressively, dollar gains would likely extend faster. Historically, fast dollar appreciation has coincided with weak global growth (see second chart below) and unstable financial markets – a greater USD rally would alter our appetite for risk assets.



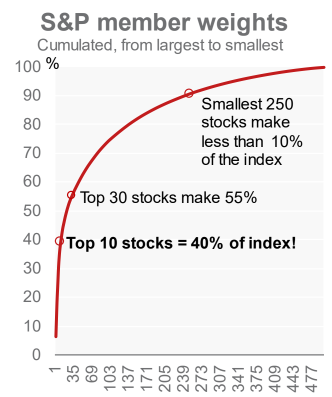
Source: BIS, Bloomberg, GenAM



Source: Citi, World Bank, Bloomberg, GenAM



Source: Bloomberg, CBOE, JPM, GenAM calc.



Source: SPX, Bloomberg, GenAM calc.

FX volatility has picked up; equity vols will follow but we see more downside for rates volatility

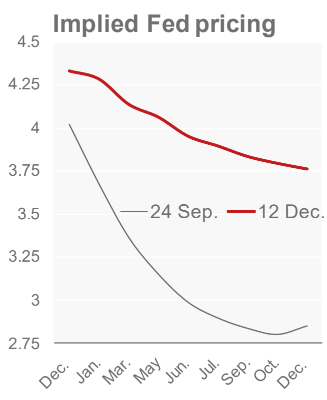
Instead, a transactional, more cooperative Trump would likely lead to profit taking on dollar longs, challenging our moderately bullish USD views. Policy uncertainty thus makes FX views more uncertain. FX volatility has started to pick up already (third chart above). In contrast, equity and credit volatility are low, on a historical basis, and likely to pick up through the 2025 surprises. The US equity market is also extremely concentrated (final chart above): the top ten stocks now make 40% of the market capitalisation of the S&P500, and the top 30, 55% – new highs. This makes US indices less diversified and more exposed to gyrations in a small number of stocks. In contrast, our view that rates volatility would start to normalise in 2024 has proven right. The MOVE index is trading at the lowest level since early 2022. We see room for further normalisation there through the rate cut process. Arguably, inflation uncertainty is such that rates volatility will not return to the pre-Covid lows. Still, nominal rates volatility is currently too high relative to inflation breakeven volatility (the former may fall even as the latter rises).

Long yields skewed to the downside, if not much

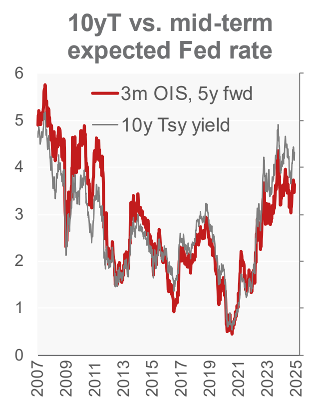
Treasury valuation slightly cheap, but US inflation risks leaning to the upside, hence too early to embrace long US duration

The inflation debate is still on. The US core CPI has jumped from a 3-month annualised pace of less than 1.6% in July to 3.66% in November. We suspect that the short cycle of gyrations will see better news in the coming months, but the persistent resilience of the US economy, low unemployment, and positive output gap (CBO estimates that GDP is now just over 2% *above* potential, a high level historically which contrasts with the negative gap when Trump came in eight years ago) all imply upside risks, which Trump policies will not assuage.

The good news is that Fed expectations have already repriced aggressively (bottom left chart below), with only just over 50bp of cuts priced for 2025 (we have 75bp in our books). Also, the market-implied Fed rates 5 years down the road is just above 3.60%, which looks high relative to our own estimate of nominal neutrality. The Fed has its long-term dot at just 2.90% (which looks slightly low and may continue to be revised higher). Then 10-year Treasury yield itself is now trading about 70bp above this 5y3m OIS rate – a high spread by historical standards, which arguably owes partly to the large cheapening of Treasuries on an asset swap basis (largely completed, we reckon). In all, we expect Treasury yields to close slightly lower than forwards in 2025, but we will start the year with a cautious or even somewhat defensive view on US duration.



Source: Bloomberg, GenAM



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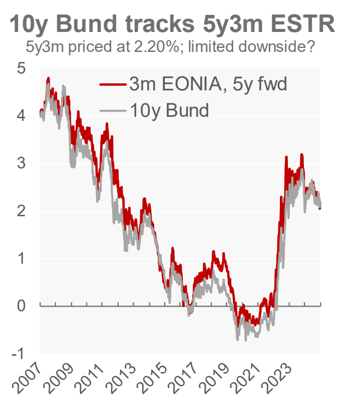
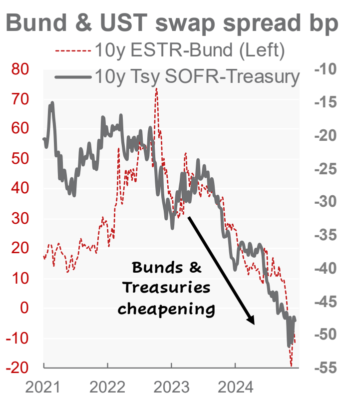


Source: Bloomberg, GenAM



Source: Bloomberg, GenAM

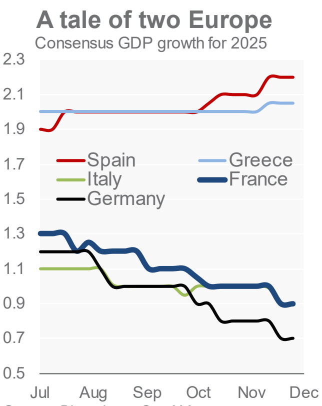
We are slightly more constructive on EUR duration at the turn of 2024-25, given the more balanced EA inflation risks. The negative output gap, weak demand and Chinese deflationary winds offset the risks coming from sticky service inflation and

Long EUR yields skewed to the downside, if by not a lot. Prefer the belly (10y) to the wings

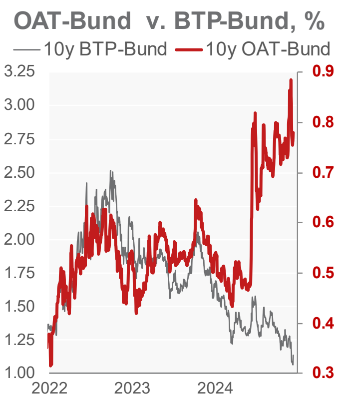
ongoing wage pressure. Bund valuation is not so exciting, with the market currently pricing the ECB at about 2.20% in 5 years – close to our fair value estimate. Still, with the ECB set to undershoot neutrality in the current cycle, we see room for that implied rate to move down in 2025. In all, with the Bund having also cheapened massively on a swap spread basis, and the election likely to deliver only a limited fiscal expansion (market talk on this looks exaggerated), we see yields skewed to the downside, if not by a lot. With rates volatility set to erode, expect the 10-year sector of the curve to outperform the wings (2-5y area and 15y+ combined).

OATs too risky until elections hopefully unlock the political gridlock

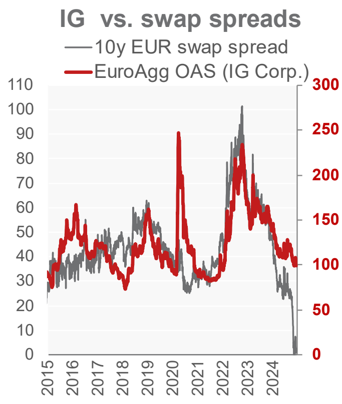
French OATs offer a large pick-up vs Bund, at 77bp in 10-year as we go to press. Is this an opportunity or a risk for investors? We suspect the political and fiscal situations will stay fragile in 1H25. Although President Macron has expressed a preference for avoiding another dissolution into the end of his term (2027), we expect another French general election in summer 2025. Only then a clarification of the political situation may improve the OAT outlook.



Source: Bloomberg, GenAM



Source: Bloomberg, GenAM



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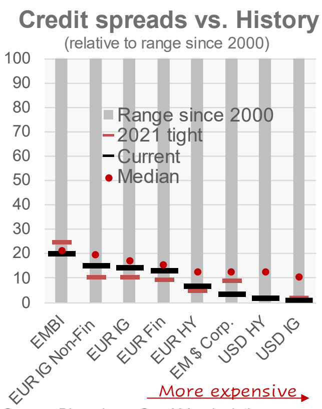


Source: Bloomberg, GenAM calculations

Positive credit still, moderately long equities

Our structural credit long coming to test. We have for long expressed a preference for Credit over Govies, both for carry and the belief that the risk-free status of government bonds was being compromised: sovereign debt metrics have deteriorated significantly over the past 16 years (especially through the GFC and pandemic). Corporate bond spreads are now trading at very tight level vs. Govies, particularly so in the US (right chart above). However, the picture is different when looking at Credit relative to swaps (third chart above). One point of attention is the revival of the M&A cycle, which seems to have started and, in the US, will be supported by the combination of rate cuts, deregulation and tax cuts. This may imply, down the road, some re-leveraging, and a deterioration in corporate fundamentals. Still, for now we continue to like the carry in credit, though our overweight remains larger in Investment Grade than High Yield (see Credit section for details).

Treasury valuation slightly cheap, but US inflation risks leaning to the upside, hence too early to embrace long US duration

EM Hard Currency debt more insulated to tariffs than local markets

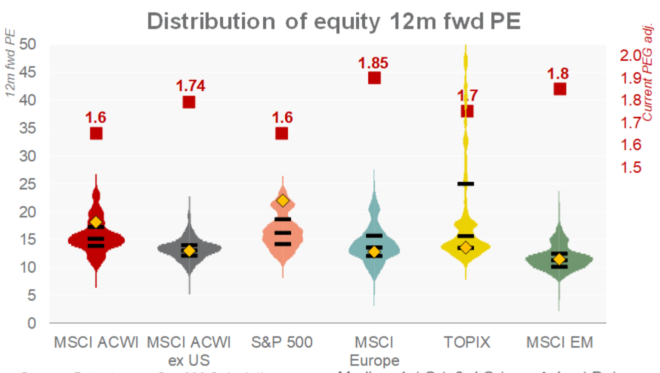
Emerging markets face challenges under Trump, along with international trade. National exposures contrast heavily, e.g. the commodity exporters look relatively more insulated. Regionally, Asia is most exposed to a rise in tariffs. Importantly, Asia takes only a low share of the Hard Currency EM debt indices, as opposed to Local Currency Debt and Equities (both heavily dominated by China). Our preference in the EM Fixed Income space goes for Hard Currency debt, as opposed to Local and FX.

Positive on equities, with higher vols

Stretched equity valuation? Only to some extent. The left chart below offers a good summary of valuation. Yes, at 22 times the profits of the next 12 months, the S&P is dear relative to history. Yet correct this by long-term profit growth and the relative cost and return of capital, and valuation no longer appears extreme relative to other markets. Europe, at about 14 times the profits of the next 12 months, is not particularly expensive. The macro environment of ongoing growth and central bank rate cuts is conducive. Also, massive inflows into Money Market Funds should start to reverse by mid-2025, as the rate cuts bite into returns, which should underpin both equity and bond funds. Small caps, still cheap, are well positioned to benefit (final chart).

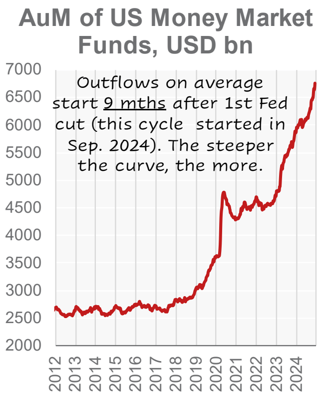
> Macro environment rather supportive for equities, but we expect a significant rise in volatility

In all, we turn the year with a small overweight in equities, good international diversification (balanced US/EU, prefer equal-weight S&P, long Europe ex-EMU, "made-in-USA" Europe, India etc) and a cyclical bias – see the Equity section for details. We however expect equity returns to reach a lower gear next year and over the medium run, as recently advertised in our annual Capital Market Assumptions report: '[Shaving expectations – our new 5-year return forecasts]'. As discussed above, we also expect greater equity volatility in 2025 on valuation concerns, higher policy uncertainty, higher concentration. Both the US yield curve and long-term US real yields, that equity volatility tends to lag, also point in that direction.

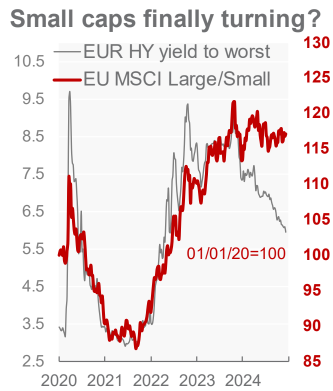


Source: Datastream, GenAM Calculations

Note: data shows distribution of multiples over time, starting from 1995 or later if not availables. Numbers refer to BEst PE 1FY
■ = PEG adjusted: PE corrected for expected EPS long-term growth, ROE and cost of equity (COE)



Source: ICI, Bloomberg, GenAM



Source: MSCI, Bloomberg, GenAM

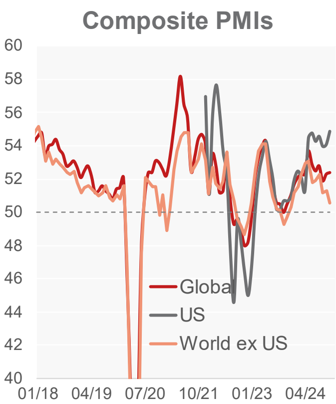
MACROECONOMIC OUTLOOK

Thomas Hempell, Guillaume Tresca, Martin Wolburg, Paolo Zanghieri

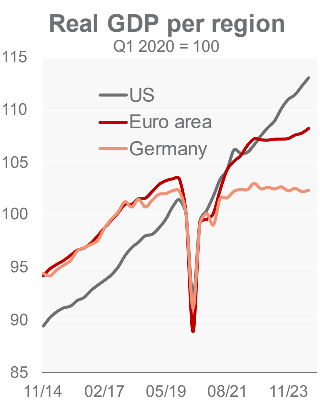
- **We anticipate world growth to remain resilient in 2025, if with marked regional differentiation. The booming US economy is set to slow only moderately. Consumption remains solid, productivity continues to grow, the credit cycle is supportive and likely Trump 2.0 tax cuts will underpin investment.**
- **This contrasts with a Euro Area (EA) economy burdened by political and trade uncertainties which makes an only tepid recovery likely in 2025, led by Southern Europe.**
- **New policy measures in China will help to cushion the drag from the property crisis, sluggish consumption, and looming trade risks, but thus far undershoot the scale needed for a robust recovery.**
- **Disinflation continues. The balance of price risks is mildly tilted to the upside in the US but much more two-sided in the euro area where sticky services inflation is increasingly balanced by increased cyclical risks.**
- **Following a likely 25bp rate cut in December, we expect another 75 bp of rate cuts by the Fed in 2025 to a terminal 3.5-.75% range. The case for further easing is even more clear-cut for the ECB. We expect sequential 125bp cuts in 2025 to a landing rate of 1.75%. PEPP reinvestment will be terminated in full from 2025 onwards, accelerating the reduction of sovereign debt holdings at the ECB by about €7.5bn/month.**

A resilient global growth outlook for 2025 overshadowed by political and trade policy uncertainties

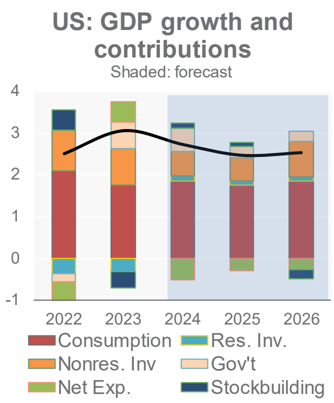
The global economy starts 2025 on a resilient footing. Yet it is marked by striking divergences and overshadowed by policy uncertainties. After shrugging off the effects from massive and synchronized rate hikes remarkably well in 2024, the global economy is headed for 2025 as another year of moderate growth. Receding inflation and a continued catch-up in nominal wages will continue to underpin real disposable income, bolstering consumption. Continued rate cuts and likely US tax reductions bode well for investment. Yet high political uncertainties (snap elections Germany, toppled government in France) and fiscal consolidation will burden sentiment in the euro area. And the risk of punitive tariffs under Trump 2.0 is a major worry for manufacturers mainly in China and major trading partners of the US, including the EU. This also implies that services will continue to lead economic expansion in advanced economies, whereas manufacturing may remain in the doldrums for another year.



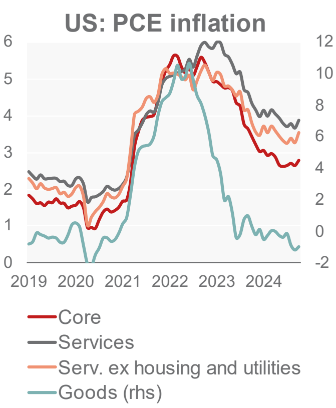
Source: Datastream, GenAM



Source: Datastream, GenAM



Source: BEA, GenAM



Source: BEA, GenAM

Moderate economic expansion, receding wage pressure and cheapened energy prices will support further disinflation. This will allow central banks in the advanced world to cut rates further, even if landing rates to be reached in 2025 will remain significantly higher than over the pre-Covid decade. The risks around the disinflation path

Disinflation has more legs, with risks still tilted to the upside in the US while more two-sided in the euro area

inflation diverge. They are still tilted to the upside in the US (robust economy, inflationary Trump policies) while much more two-sided now in the euro area (sticky services inflation contrasting higher cyclical risks). Emerging markets are still set to enjoy healthy expansion amid eased inflation and lower US rates, though US tariff risks, a strong US dollar and China's structural problems (property crisis and subdued consumer confidence) will keep a lid on growth.

Extended US exceptionalism

President Trump inherits a strong US economy. We expect GDP growth to moderate only mildly from 2.8% to 2.4% next year. Our growth forecast is above consensus as we expect that the new administration will prioritise next year pro-growth policies like tax cuts over more controversial ones like pledged massive immigration curbs and sharp tariff increases. This tilts the balance of risks towards less benign outcomes.

GDP growth at 2.4% in 2025, with policy related downside risks.

Growth will remain chiefly driven by consumption, in turn supported by a strong labour market. Data for the end of the year show that, while job creation has moderated, layoffs remain below what one would expect given the past tightening in borrowing costs. We expect the unemployment rate to peak at 4.4% by mid-2025, a marginal increase from the 4.2% posted in November, as strong activity and labour hoarding will limit dismissals. On top of that, we expect a pick-up of investment, favoured by the continuation of robust profitability, easing financial conditions in a context of healthy demand and the delayed effect of the Biden administration's industrial policies. The sharp increase in structures investment in the computer and electronics sector seen over the last couple of years should be followed by higher equipment spending. AI will likely provide an additional boost, although this is difficult to quantify as sufficiently detailed information is not available yet. Unpredictable trade policies constitute a key downside risk for capex.

Capital accumulation would allow the string of good productivity data do continue. Stronger productivity is likely to have pushed the trend growth rate of the economy above 2%. This should mitigate the inflationary pressures from domestic demand, but, as shown by the end-2024 data, disinflation will remain very gradual and subject to bouts of volatility. We expect core PCE inflation to end 2025 still slightly above the Fed 2% objective. Risks are tilted to the upside, as service inflation may provide stickier. In particular, the past moderation in house price growth has stopped and this could delay and dampen disinflation in rents.

Fed to cut by no more than 75bps in 2025

This will force the Fed to a cautious proceeding. Our baseline has three rate cuts, spread over the year, leading the Fed funds rate to end 2025 in the 3.5%-3.75% range with the risks tilted to fewer cuts. Stickier inflation coupled with healthy domestic demand would not require much loosening. Moreover, we expect the FOMC to continue to raise its estimate of the neutral rate, currently at 2.9%, given stronger trend growth and the widening budget deficit.

EA: Muted recovery amid looming tariffs and policy uncertainty

Indicators suggest weak growth in the winter half

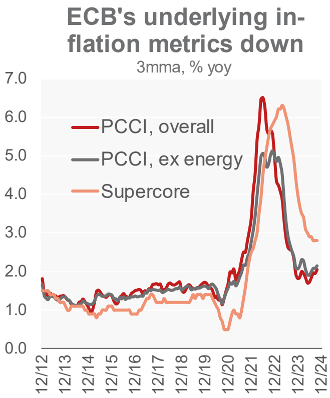
The euro area recovery still looks shaky. Following a healthy 0.4% qoq growth in Q3, sentiment indicators point to much shallower growth in the final quarter of the year. Expectations of firms and consumers worsened again. This might be due to some indications of labour market cooling in the presence of a still low unemployment rate of 6.3%. Policy uncertainty amid political stalemate in Germany ahead of snap elections in February and the recent breakdown of the French government will weigh on business and consumer sentiment. Also, the threat of US import tariffs keeps trade uncertainties high. If introduced in full they would hit the already pressured German car industry very hard, adding to the structural problems of the euro area's largest economy.

Activity to improve but to stay subpar in 2025

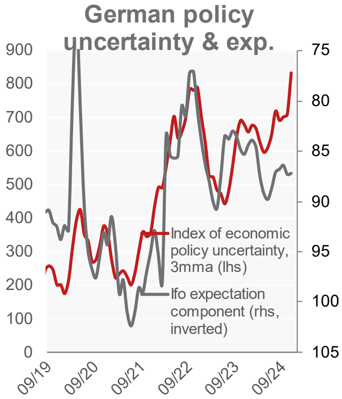
That said, we still expect a mild recovery that may gain some momentum over the course of the year. Receding inflation amid still solid wage increases will back real income growth. There is indication that monetary policy easing increasingly feeds through to the economy. Vigorous growth in the US will help the very much export-oriented economies. We look for somewhat strengthening activity from Q2/25 onwards but do not expect quarterly growth rates to exceed potential. Annual growth is set to stay at 0.8% in 2025, well below the consensus expectation of 1.1%.

ECB to lower key rate in outright expansionary territory

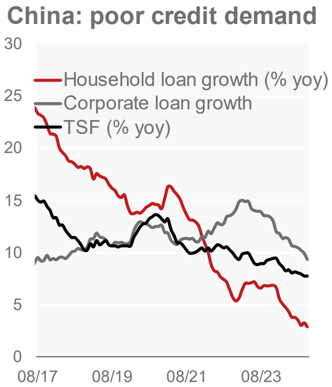
Looking through the temporary inflation spike in the last quarter of 2024, inflation will continue to recede. Core inflation was at still 2.7% yoy in November, but moderating wage growth, the completed passing through of the past inflation shock and subpar growth will drive underlying inflation towards target in 2025. This will allow the ECB to further ease monetary policy. With a key rate of 3.0% after four 25 bps cuts, it is still slightly restrictive. With inflation risks now much more two-sided we expect the ECB to push its key rate into outright expansionary territory until 1.75%, most likely by means of 25 bps cuts at each of the subsequent meetings until July.



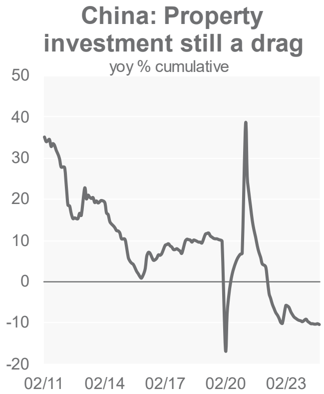
Source: Datastream, ECB



Source: Datastream, GenAM



Source: Bloomberg, PBoC, GenAM



Source: Bloomberg, NBC, GenAM

China: slowing down despite new monetary and fiscal supports

China: tariff the main risk that can intensify deflationary pressures

China will continue to face numerous challenges in 2025 from deflation, poor consumption, an ailing housing market to looming US tariffs. Growth is thus expected to slow to 4.5%, from 4.8% in 2024. However, uncertainty is high, fueled by the new US policies under Trump 2.0 but also by the new Chinese policymaker's economic strategy. High frequency indicators have recently shown an improvement in business and consumer sentiment. The Politburo having pledged more policy support which is needed for a sustained recovery of demand. At least, the support will reduce downside tail risks in 2025 but deflationary pressures are here to stay, and the housing market recovery will be protracted. Thus, we expect a further 25bp cut of the main policy rates with a skew for more cuts and a fiscal support between 1-2ppt of GDP per year. US tariffs are the main wild card. China is in a worse shape than in 2017/18 during the first round of US tariffs even if they have adjusted their supply chain. Tariffs would increase industrial overcapacity and deflationary pressures.

GOVERNMENT BONDS

Florian Späte

- **US yields still have some upside potential in the short term. As the year progresses, falling inflation and weaker growth combined with further key rate cuts should support a pullback in yields.**
- **The trend of retracing Bund yields is likely to continue. Given reached levels, however, the momentum will slow; we forecast a decline to 2.0% for 10-year Bund yields by end of 2025.**
- **The ECB's key rate cuts, a slight acceleration in growth during the year and a further decline in bond market volatility mean that the environment for euro area non-core government bonds remains favourable in 2025. However, a further increase in the net-net supply of government bonds and political uncertainties in several euro area countries lead us to expect a moderate widening of spreads in 2025.**

Hump-shaped trend in US long-term yields expected to emerge in 2025

Expectations that Trump will win the presidential election and continued robust economic data have pushed US yields higher since September (driven by both higher real yields and rising inflation expectations). However, uncertainty about what policies will be implemented remains high and is likely to persist. While we do not expect Trump to fully realise all the proposals currently on the table (including tariff increases, immigration bans, deregulation, tax cuts), we still see potential for a further rise in US yields in the near term. Given the levels reached and the recent marked reduction in expectations for further Fed rate cuts (only 80 bps are priced in by the end of 2025), we see the November peak of 4.5% for US 10-year yields as the upper limit. We think higher yield levels are only conceivable if Trump implements the policies that particularly drive up inflation quickly and across the board.

In our baseline scenario, however, we expect yields to decline again over the medium term. Core inflation is still expected to be above the 2% target at the end of 2025, but this represents a decline from today's levels. In addition, growth, which is currently above trend, is likely to slow. In our view, this will prompt the Fed to cut key rates a little more than financial markets currently expect. We forecast the Fed to lower the federal funds rate by 100 bps to 3.75% by the end of 2025 (assuming the new US administration does not go "full on"). For 10-year US yields, we expect a level of 4.10% at the end of 2025.

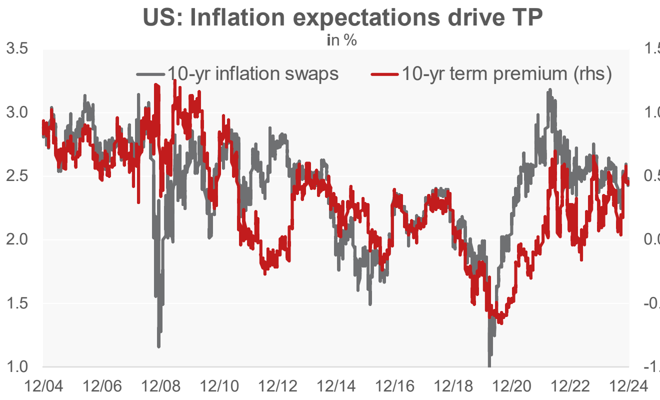
Structural changes keep US yields at elevated level long term

We consider an even larger yield decline to be unlikely. On the one hand, the budget deficit will remain high in the future (the US government's interest payments alone will amount to around $ 1000bn in 2025), which will lead to a high net supply of US Treasuries. According to our estimates, the private sector will have to absorb a volume of up to $ 1800bn in 2025. On the other hand, the term premium – a key determinant of long-term yields alongside the expected key rate in the medium term – will remain in positive territory given the sustained increase in inflation uncertainty.

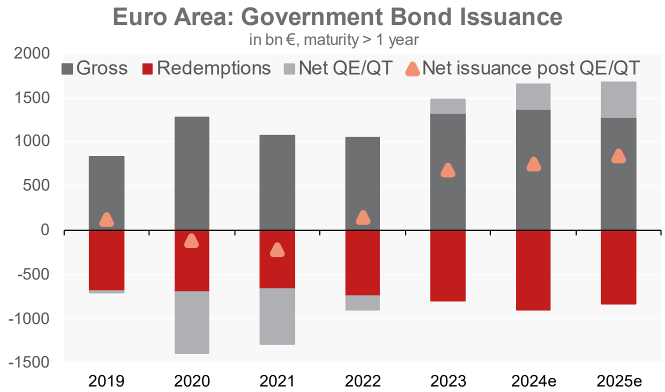
By contrast, we expect yields on 10-year Bunds to fall further in the short term, leading to a further widening of the transatlantic yield spread at least in Q1 2025. Not least, an imminent trade conflict with the US will confirm the ECB's policy of cutting rates. We expect five further steps of 25 basis points to a deposit rate of 1.75%. Although our forecast is not significantly different from the markets' expectations, a drop below the neutral key rate level (which we see between 2.0% and 2.5%) is likely to leave its mark. The current uncertain political situation in some euro area countries (e.g., FR and DE) may also contribute to further buying of Bunds, which are perceived as a safe haven. By the end of 2025, we see 10-year Bund yields at 2.00%.

Decline in nominal yields in the euro area due to lower real yields

The forecast decline in yields should be entirely due to lower real yields. At currently 0.3%, 10-year real yields are 25 bps higher than at the start of 2024. This conundrum is likely to unravel. By contrast, 10-year inflation swaps have fallen below 2.0%. However, the green transition of the economy, declining labour potential and rising military spending do not mean that the low inflation environment of the 2010s is likely to return. Moreover, the first negative inflation risk premium since 2021 is not sustainable and is likely to rise again in the medium term.



Source: Bloomberg, GenAM



Source: Bloomberg, Datastream, GenAM

Despite favourable environment, little leeway for spread tightening

Euro area non-core government bonds have performed impressively in 2024. The environment, characterised by further ECB key rate cuts, a moderate acceleration in growth (from an albeit low level) and a further decline in bond market volatility (currently only slightly below the long-term average), is forecast to remain favourable in 2025. The financial market environment, which we expect to remain fundamentally benign, is also favourable for non-core bonds.

Given the low spread levels market participants are advised to invest prudently

The main argument against further spread compression is simply the low levels that have been reached. Spreads over Bunds in most countries have recently fallen to long-term lows. They are below levels that we consider fair and have little potential for narrowing. The challenging government bond supply situation also calls for some caution. Although the uncertainty regarding the supply to be absorbed by the private sector in 2025 is unusually high given the political situation, especially in some larger euro area countries, it can be said that the reduction in gross supply by € 100bn (reduction in net issuance by € 30bn and € 70bn in redemptions) to around € 1270bn will not be enough to compensate for the ECB's Quantitative Tightening, which is gathering pace. As the ECB will not only stop reinvesting PSPP bonds in 2025 (as already in 20024), but also no longer roll over maturing PEPP bonds, the central bank is withdrawing over € 400bn from the market- € 125bn more than in 2024. Accordingly, net-net supply (including the ECB) will rise to almost € 850bn.

French OATs will remain in the spotlight in 2025. As stated above, the political crisis in France has not yet led to contagion, but other bonds have even benefited from a substitution effect. Although the OAT/Bund spread is currently above fair value, we still advise caution. The political stalemate in parliament will not be resolved until at least the middle of the year. Even if a stable government can be formed, we see reducing the budget deficit as an extremely difficult challenge. Further pressure from the financial markets (i.e., rising spreads) is even more likely as there is no sign of a majority in parliament for a consistent and rapid consolidation of public finances.

CREDIT

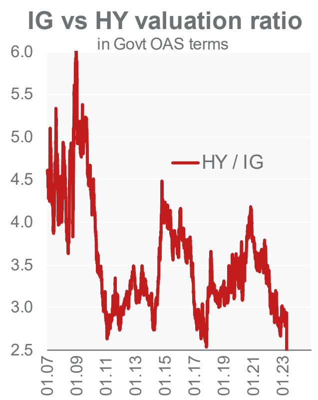
Elisa Belgacem

- **We reiterate our preference for Credit over Govies in 2025. The OAS vs ASW ratio is at its tightest since 2003, with total return investors focusing on OAS and MtM managers on spread vs swap. Carry is attractive given the strong fundamentals and long duration, especially for funds moving from monetary placements. We expect credit spreads to evolve around current levels in 2025.**
- **We run a long IG and mild HY overweight: Defaults are decreasing rapidly in the bond space but not in loans, indicating a two-speed credit world. Large companies have diversified liquidity sources, while smaller ones remain vulnerable. Private debt liquidity is ample but concentrated in large funds. We prefer IG and to a lesser extent HY and private debt, and underweight the leveraged loan market.**
- **We overweight Non-Financials vs Financial: the financial sector, representing 40% of IG, is fundamentally performing well with low NPLs. However, it is exposed to sovereign risk, with challenges in France, Germany, and potential impacts from US financial deregulation.**
- **We turn slightly more constructive on cyclical sectors: Corporate fundamentals remain strong with lower volatility compared to peripheral government spreads. However, modest credit rating deterioration is expected due to pressure on cyclical sectors and increased M&A activity. We upgrade IG Autos to OW and keep our long position on Real estate.**

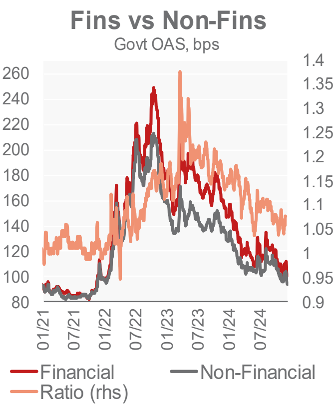
Elevated all-in yields continue to drive strong demand. Credit spreads have tightened significantly in recent weeks due to reduced supply during the holiday season. However, demand remains strong as investors are attracted by the high all-in yield, particularly in view of the expected decline in yields on monetary products.

Fundamentals to remain under control

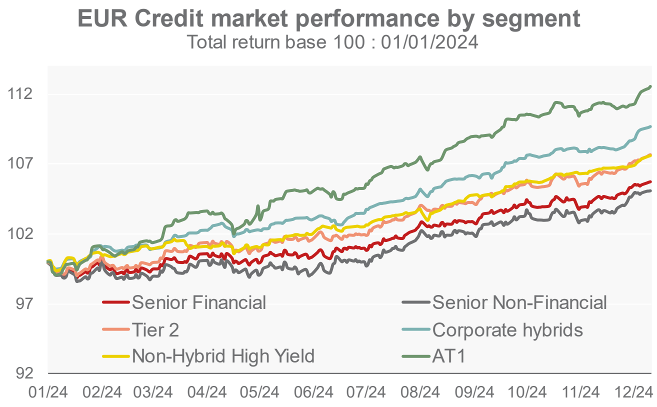
Defaults in both the US and Europe have been on a slow declining path since mid-2010, which is positive. However, fundamentals have only started to deteriorate as rating agencies have started to take a cautious stance on the most cyclical European companies, either by downgrading ratings or revising outlooks downwards. We believe that the downside risk is limited and that the highest downgrade risk is in the single B or CCC space rather than investment grade. The wild card, of course, is the potential pick-up in M&A activity, which could occasionally lead to downgrades in credit metrics. However, even if some deals lead to very visible downgrades, we are not overly concerned that a large acquisition will worsen credit metrics for the credit class as a whole, as 1/ most deals don't change credit metrics and 2/ M&A usually



Source: Bloomberg, BofAML Indices, GenAM own calculations



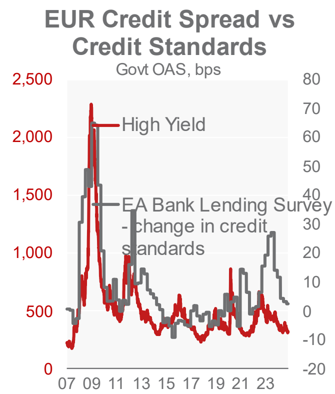
Source:Bloomberg, BofAML Indices, GenAM



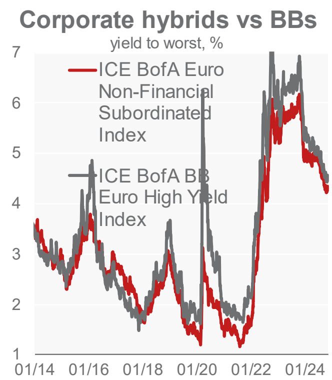
Source: Bloomberg, BofAML indices, GenAM consists of IG companies acquiring HY companies, the former usually having more room to manoeuvre, which traditionally improves the overall credit quality of the market.

Turning more positive on cyclical sectors

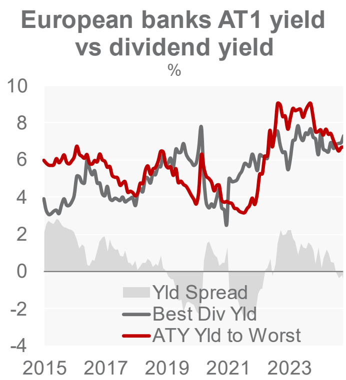
In the first half of the year, the cyclical premium in credit markets was extremely low. This started to change over the summer months as the companies most exposed to the economic cycle underperformed, in particular the automotive sector. The transition to electric vehicles, intense competition from Chinese manufacturers and sluggish demand from China pose significant challenges. However, we believe that most of the bad news is already priced in. We are therefore shifting from a defensive sector allocation to a more balanced one, in the expectation that investors will start to chase market laggards as demand for credit remains strong into the new year.



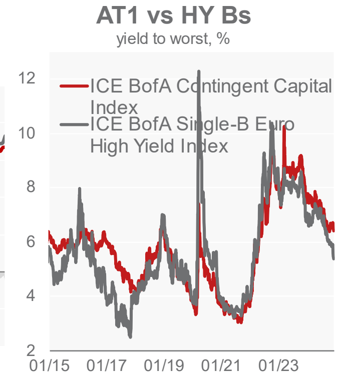
Source: Bloomberg, BofAML indices, GenAM



Source:Bloomberg, BofAML Indices, GIAM own calculations



Source:Bloomberg, BofAML indices, GenAM own



Source:Bloomberg, BofAML Indices, GenAM own calculations

Little margin for error but carry still appealing

Looking at historical valuations, credit looks expensive versus the Bund, but this is much less the case when looking at credit versus swaps. Similarly, the volatility adjusted carry versus similarly rated government bonds remains much more favourable for credit than for govies. In our view, this reflects a convergence of risks since Covid, as government debt has soared while corporate leverage has been stable, if not falling. We believe that the delicate political situation in several major European countries will make trading long credit versus govies even more profitable in 2025, despite a tight starting point for credit spreads.

We expect credit spreads to hover around current levels in the coming months, maintaining elevated carry. Valuation considerations favour Europe over the US. We prefer long IG and subordination risk to pure HY, while maintaining a slight overweight in HY. HY valuations are more expensive than IG and, as explained above, we believe that fundamentals are also more fragile in HY than in IG. We also prefer subordination risk to credit risk in 2025.

Underweight Financials versus Non-Financials on politics

However, our long credit position is skewed towards non-financials. Indeed, the three largest countries in the European IG financial index are France, the US and Germany. The unstable political situation in France is likely to eventually weaken its so far impressive resilience to the increased volatility of the OAT-Bund spread. Despite this, in the subordinated space, where we continue to favour AT1 as we believe that the high carry is going to continue drive elevated total return performance.

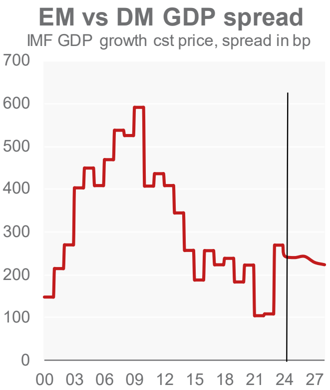
EM SOVEREIGN CREDIT

Guillaume Tresca

- **The outlook remains supportive despite greater uncertainty. Sound macroeconomic fundamentals will provide shield against the Trump's policies. We expect positive EM sovereign fixed income return in 2025.**
- **US tariffs are the main risk, but the impact will be heterogenous across countries and only visible from H2 25 at the earliest. Trade tensions will lead to more regionalisation.**
- **EM external debt is in the best position to benefit from the US exceptionalism. Not all rating buckets are expensive, and US credit provides a strong anchor to EM spreads. EM local debt will likely suffer from Trump policies. That said, EM rates can perform, especially in CEE, but EM FX will remain on a back foot vs. the USD.**

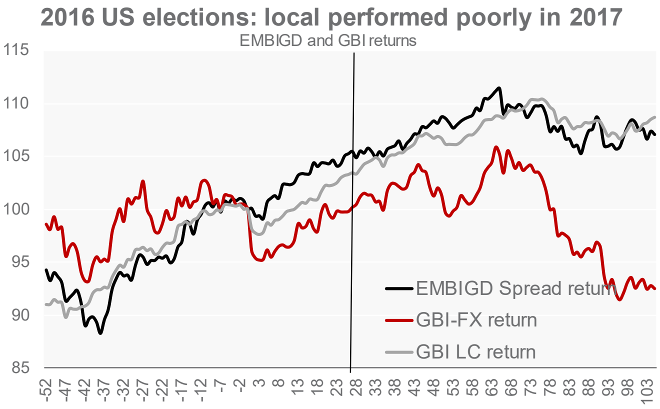
Sound macro fundamentals to provide a shield against higher uncertainty.

A resilient setup with more headwinds but positive returns. EMs will remain resilient in 2025, despite more challenges after the US Republican sweep. Unlike in 2016/2017, EMs are in a better position, and we do not expect their macroeconomic fundamentals to deteriorate. Indeed, GDP growth is set to be stable 4.2% according to the IMF, still above the pre-pandemic average and well above DM. Recent activity indicators have been supportive, and EMs will continue to benefit from US exceptionalism and robust US growth. US tariffs are the main risk, but it is currently difficult to assess their actual impact. The real impact will be visible in the long term, probably in late H2 25 or even 2026. Even if the outlook is somewhat less favourable, sound fundamentals will provide some protection and may even lead to upside surprises. Indeed, on average, external vulnerabilities are limited, private sector balance sheets are sound, FX reserves are ample, and central banks have pursued proactive policies since the Covid. They are indeed well advanced in the cycle. This means that they will have room to manoeuvre in the event of financial instability or a growth slowdown. In this respect, we continue to expect positive returns for EM fixed income next year.



Source: Bloomberg, IMF, GenAM

Source: Bloomberg, IMF, CPB, GenAM



Source: Bloomberg, GenAM

EMs under Trump: more uncertainty

Trump's policies will bring more uncertainty, but EMs are better prepared than during his first term. Trumponomics will affect EMs through three main channels. First, the main risk is new tariffs: their impact will be heterogeneous, with only a few countries affected in our central scenario, but will lead to more regionalisation in trade flows. EM ex-Asia should hold up better, with Asian manufacturing exporters (China, Vietnam, Malaysia) and Mexico likely to be most affected. Headlines news can be numerous, but they will not be necessarily followed by action. Second, an opportunistic foreign policy could hurt CEE and Ukraine but benefit Turkey as a pivot state.

Third, a bolder approach to immigration and a tax on remittances would hurt Mexico and Central American countries.

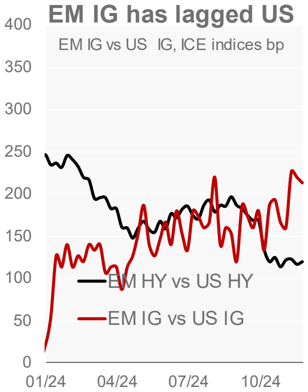
External debt: still attractive return in 2025

High return for EM external debt benefiting from US growth. Mind higher UST rates in the short term

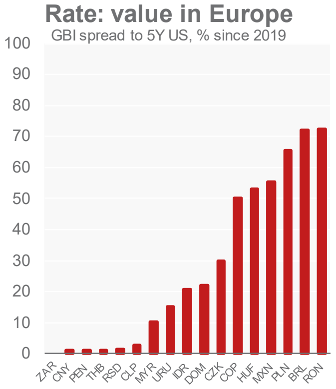
We expect a high single-digit positive return in 2025 as external debt is best positioned to benefit from US exceptionalism, resilient EM growth and a still positive risk environment. With higher uncertainty and tariff-related headlines, spreads will initially widen. However, the risk of large spread widening is limited if US credit does not widen significantly. The strong appetite for it provides an anchor for EM credit spreads. Moreover, EM credit is cheap vs US one and this can fuel US crossover inflows into the asset class.

Valuations have been tight for some time, but not everything is expensive. We continue to see value in the B and CCC buckets. BBs are historically expensive, but for good reasons as fundamentals have improved. In this bucket, we like Morocco, Serbia and Colombia. IG names have been rich, but we see opportunities in Romania and Mexico when the dust settles.

The main risk to the asset class, and IG in particular, is an unexpected rebound in the US Treasury yields. Should they spike in Q1 r EM sovereign credit would perfume better later in Q2 when spreads are wider and the UST rates start to fall more meaningfully.



Source: Bloomberg, ICE, GenAM



Source: Bloomberg, JP, GenAM

12M expected positive return despite spread widening

12M TR for different rate and spread scenarios, Dgov index

	OAS spread	US 8Y 3.92%	4.02%	4.12%	current 4.22%	4.32%	4.42%	4.52%	4.62%
	126	15.8%	15.1%	14.3%	13.6%	12.9%	12.2%	11.5%	10.8%
	146	14.3%	13.6%	12.9%	12.2%	11.5%	10.8%	10.1%	9.4%
	166	12.9%	12.2%	11.5%	10.8%	10.1%	9.4%	8.7%	8.0%
	186	11.5%	10.8%	10.1%	9.4%	8.7%	8.0%	7.3%	6.6%
	206	10.1%	9.4%	8.7%	8.0%	7.3%	6.6%	5.8%	5.1%
current	226	8.7%	8.0%	7.3%	6.6%	5.8%	5.1%	4.4%	3.7%
	246	7.3%	6.6%	5.8%	5.1%	4.4%	3.7%	3.0%	2.3%
	370	-1.5%	-2.2%	-2.9%	-3.7%	-4.4%	-5.1%	-5.8%	-6.5%
	390	-2.9%	-3.7%	-4.4%	-5.1%	-5.8%	-6.5%	-7.2%	-7.9%
	410	-4.4%	-5.1%	-5.8%	-6.5%	-7.2%	-7.9%	-8.6%	-9.3%
	430	-5.8%	-6.5%	-7.2%	-7.9%	-8.6%	-9.3%	-10.0%	-10.7%

Source: Bloomberg, GenAM calculations

EM local debt: a nimble approach as EM FX to remain weak

Local debt to be affected by EM FX weakness. EM rates can perform.

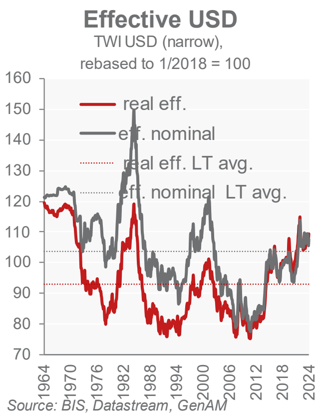
The outlook for local debt is much less supportive, given the imited Fed cuts, USD strength and strong US growth. EM local debt performed poorly in 2017 and high yield countries underperformed. That said, we continue to favour EM rates over EM FX as local rates can benefit from further central bank easing. The risk premium on rates will be higher to price in more uncertainty, but ultimately the lower UST rate will push yields lower. Again, the move will be heterogeneous across countries, and we prefer CEE rates to LatAm where central banks are less dovish. In Asia, rates have been at low levels for some time and central banks will be easing parsimoniously, so there is limited room for rates to move down. More problematic is EM FX, which will be the main transmission channel for Trump-related risks. Carry attractiveness is diminishing and USD strength will limit EM FX appreciation. However, EMs will be more resilient vs the other major FX pairs. We like the BRL vs. MXN, the TRY on a tactical basis to benefit from the very high carry and disfavour the North Asian currencies in the wake of a weaker CNY.

CURRENCIES

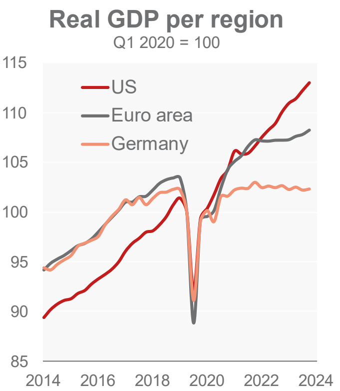
Thomas Hempell

- **The US dollar is dear on various metrics. Yet we see further moderate USD gains over 2025. US exceptionalism is set to expand over 2025, backed by continued US productivity gains. Trade uncertainties and the risk of punitive US tariffs also favour USD bids, as does the sizeable yield advantage that US markets will retain for longer. Trump 2.0 tax cuts and reshoring pressure may entice more net FDI inflows into the US.**
- **Conversely, the euro area recovery remains shallow, burdened by lost competitiveness and political and trade uncertainties. We expect a lower EUR/USD, but a fall below parity would require punitive Trump tariffs or a deeper political crisis in one of major EMU members – which is not part of our base scenario.**
- **A pick-up in US bond yield may support the USD/JPY near term. Further into 2025, however, the yen may prove the only G10 outperformer against the USD as BoJ tightening contrasts rate cuts by other major central banks.**
- **Chinese authorities are likely to accept a gradual yuan depreciation amid rising trade tensions and a broadly stronger USD. Yet worries about larger capital outflows and fresh fiscal stimulus will likely keep the decline of the tightly controlled CNY gradual.**

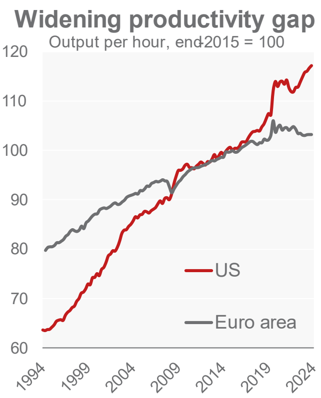
Boosted by Trump's sweep victory in the November US elections, the USD is set to finish 2024 with sizeable gains – with the trade-weighted USD up almost 7% year-to-date, thereby more than reversing the -1% weakness seen in the previous year. This leaves the USD historically dear: the inflation-adjusted real effective exchange rate exceeds its long-run average by 20% and is just 7% below its historical peak seen during the Volcker era as Fed Chair in the 1980s (left chart).



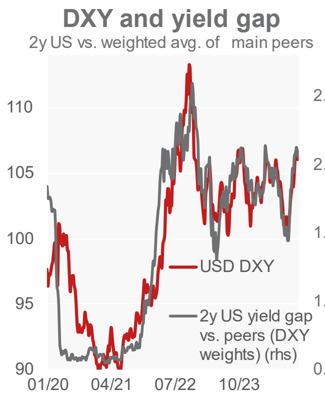
Source: BIS, Datastream, GenAM



Source: Datastream, GenAM



Source: Datastream, GenAM



Source: Datastream, GenAM

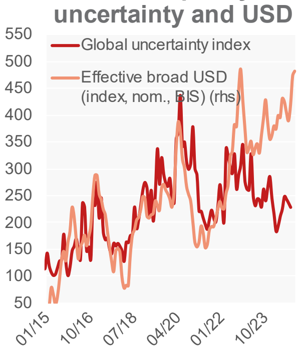
> Despite historically dear levels reached, we expect a strong dollar for longer on US exceptionalism

Such high valuation levels call for prudence. And yet we see some further moderate upside for the USD over the coming months as US exceptionalism has more legs. First, the US is set to extend its forceful recovery from the pandemic, backed by solid productivity gains (mid charts above), whereas most other advanced economies – and notably Europe – keep struggling to gain momentum. We expect the US growth to outpace the euro area again by a factor three (2.4% vs. 0.8%). Second, upside risks to US inflation will make the Fed proceed more cautiously in cutting rates. By contrast, the ECB increasingly needs to weigh cyclical risks vs. still sticky services inflation. This will keep the US yield gap vs. peers wide – a key support of USD strength over the past years. Third, even though we don't think that Trump will go 'full-on' with his agenda on tariffs, trade uncertainties and rising US/China tensions may reignite new safe-haven demand for the US dollar (left chart below). Finally, the likely implementation of US corporate tax cuts and mounting political pressures on multinational firms to re-shore production to the US may spur FDI inflows to the dollar's benefit. The risks around our core view of some further USD are high, and FX volatility may rise. A compromising approach by Trump on trade matters may render some unwinding of crowded and consensual USD long positions. By contrast, aggressive tariffs and a trade war could push the USD much higher, and EUR/USD below parity.

The EUR is burdened by political and trade uncertainties and is likely to bottom on improving growth only later in 2025

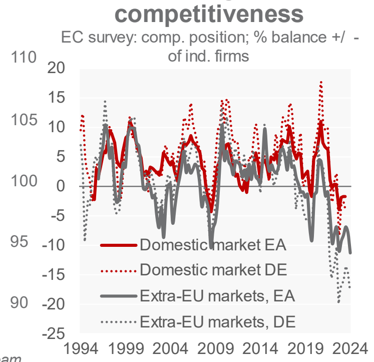
Conversely, the EUR will remain burdened by political uncertainties in France and Germany, headwinds from trade uncertainties and a severe loss of competitiveness over recent years (2nd chart below). It will probably take until at least the spring before the euro area benefits from a more visible recovery, helping the EUR/USD to bottom. That said, it seems still somewhat more likely than not that the EUR/USD will terminate 2025 on a somewhat lower level than the currently 1.05.

Global policy uncertainty and USD



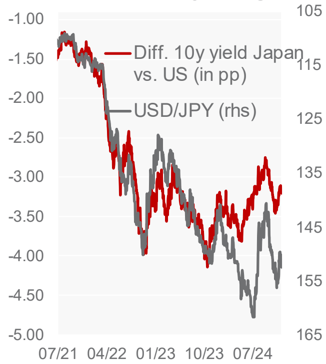
Source: www.policyuncertainty.com, Datastream, GenAM

Eroding EU competitiveness



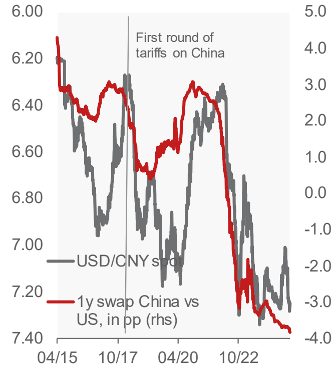
Source: EC, Datastream, GenAM

USD/JPY and yield gap



Source: Datastream, GenAM calculations

USD/CNY and rate diff.



Source: Datastream, GenAM calculations

JPY: Near-term caution, medium term upside

The Japanese yen may be the only major currency to outperform the USD in 2025. Short term, more prudence is warranted as a pick-up in US yields at the outset of 2025 may also lift the USD/JPY (mid-right chart). For the fully year, however, we anticipate the yen to strengthen. It is deeply undervalued (real effective JPY is undershooting its long-term average by >30%) and the BoJ is the only major central bank bucking the trend of monetary easing among the advanced economies. With the yield differential vs. the US set to tightening, we expect the USD/JPY headed into the mid-140s by end-2025.

JPY may be the only major currency to outperform USD in 2025

The rise of the yen, however, may be kept in check by a further fall in the Chinese yuan. Higher US tariffs and further policy easing and rate cuts in China are burdening the Chinese currency (right chart). That said, Chinese authorities will likely allow only for a gradual weakening of the tightly managed CNY on fears of massive capital outflows and a renewed setback to domestic consumer and business confidence. We have USD/CNY about 5% higher in our books by year-end at 7.50-.60.

Trade tensions and euro area political uncertainties keep the EUR/CHF tilted lower. Yet the SNB will cap excessive CHF strength with inflation already at target and the EUR may recover on the mild economic recovery forecast further into 2025. Less BoE rate cuts amid more sticky inflation pressures than in the euro area and a quite robust growth outlook may help the GBP to gain further ground against the EUR, with the higher UK carry an additional benefit. The British economy is also less vulnerable to US tariffs. Nevertheless, against USD sterling is still likely to weaken mildly

EQUITIES

Michele Morganti and Vladimir Oleinikov

- **Three positive legs ahead: resolved US election uncertainty adds to a fundamentally driven rotation out of US IT into other sectors and countries, as well as dovish CBs and a decent macro outlook, especially in the US. We add high free cashflow and increasing M&A. EMU carries more at risk but also offers much cheaper valuation.**
- **The record high in the EMU risk premium over the US may persist short term as US superior growth lingers (lower PEG), political risk stays high along with uncertainty about concrete US tax, tariff and deregulation measures.**
- **The US Q3 reporting season showed a positive EPS surprise of 6.9% (2.3% for EU) and resilient margins. In 2025, we expect a solid earnings growth of 9.7% and 8% for the US and EMU, respectively, and 6% each in 2026.**
- **We see 9-17% TR for EU and 4-8% for the US over 12 months. Short term we slightly prefer US over EMU. Later on, EMU is to benefit from higher TR potential, stabilising growth, the Chinese stimulus and a possible Trump-induced wars' ceasefire. Neutral US IT; OW EU ex-EMU, EU small cap, UK FTSE 250, Japan, slightly China, India and Malaysia. Diversify US into equal-weighted SPX & Russell 2000. Add M&A, Trump and *EU made in the US* baskets.**
- **EU sectors – maintain a cyclical tilt: OW Financials, Semis, Aero&Defense, Construction, Pharma, RE plus Food retail, HPP, Retailing, Tlc. UWs: Autos, Energy, Comm. Prof. Svs., Durables, Food, Media, Transportation, Utilities.**

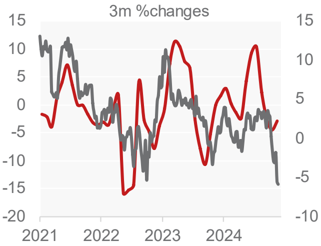
Moderate overweight (OW) in equities, with three legs to be at work

We are positioned with a moderate overweight (OW) in equities as we see three legs to be at work: the post-election cycle is usually positive, the Fed's easing one is too, and we see a continued rotation from US Tech into ex-Tech sectors and countries. US macro momentum holds well and we see for the EA one normalising growth and a pick-up in capacity utilization ahead. Additional positives: possible outflows from MMF into riskier assets, good US margin momentum (justifying current high multiples), large free-cash flow gap vs. CAPEX, improving financial conditions, rising M2 and constructive view on credit, lastly, a positive equity-bond ML model outcome.

Overall, in 2025 we see an earnings growth of 9.7% and 8% for the US and EMU, being under consensus only for the US by 4%. EMU risks are on the downside. Earnings growth should decline to 6% for both indices in 2026, where we are below consensus by 10% in the US and 5% for the EMU.

MSCI EMU 12m fwd EPS & IFO

3m %changes

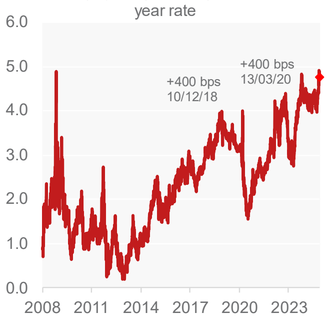


IFO exp. in 6m (2m lag of 1Q %cng)
MSCI EMU EPS (12m fwd 1Q %cng, rhs)

Source: Datastream, GenAM

Risk premium delta: MSCI EMU minus S&P

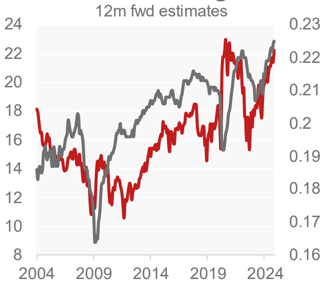
earnings yield (12m fwd) minus 10 - year rate



Source: Datastream, GenAM calculations

S&P 500: PE & EBITDA margin

12m fwd estimates



S&P 500 PE (12m fwd, lhs)
S&P 500 EBITDA (12m fwd)

Source: Datastream, GenAM calculations

12m targets (as of 11.12.24)

Market Index	composite LT models (Shiller approach for US)	of which: PE-based valuation	CAPE yield gap vs real yield 1yr fwd spread, % to avg since 2003
S&P 500	**6,000 - 7,000**	**0.9%**	**-2.0%**
MSCI EMU	**10.7%**	**17.6%**	**-0.2%**
FTSE 100	**15.8%**	**17.8%**	**0.5%**
SMI	**16.8%**	**17.1%**	**0.2%**
TOPIX	**13.7%**	**11.4%**	**-0.1%**

Source: Datastream, Bloomberg, GenAM calculations

Note: LT models: PE tgt (US 21x, EMU 13.5x, JP 14x), Fed model, EY-BY, DDM, and 3-stage eps growth model
excess CAPE yield = 1/CAPE - (10yr rate - avg inflation over 10yr)

Markets are fully pricing Trump policies and earnings rotation. EMU stocks and renewables still deserve some risk. Trump basket overperformed earnings trend meaningfully in 2024, but the price could rise further following EPS trend.

OW EU ex-EMU, EU "made in USA", Japan, small caps, M&A baskets, China, India, and equally weighted SPX

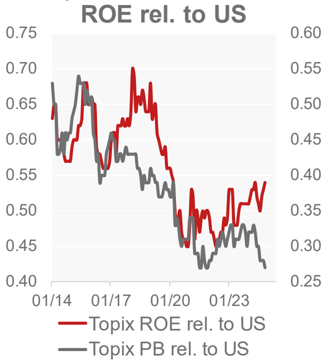
US financials, small caps and energy should continue to benefit. Renewables and IRA beneficiaries are at risk. The rotation out of Tech should also continue. The sector is penalised by very high positioning, EPS growth normalisation (from very high level), high 10-year rates for longer, antitrust risk, plus supply chain and export/trade frictions. We maintain a neutral stance on AI & US Tech due to good short-term earnings momentum and slight undervaluation vs. SPX (PEG). But, as said, earnings growth for Mag 7. is on normalization path, while S&P 493 and the extended global AI basket should see a pick-up. We suggest diversifying out of US Tech into Russell 2000 (Trump policies, lower valuation and positioning, good US macro, better small business confidence, NFIB, lower cost of credit) and SPX equal weight or SPX 493.

Impact from Trump policies will be company specific: much brighter perspectives are for EU firms producing in the USA (OW). Our *trade fear* indicator suggests that EU cyclicals are still exposed to trade risks. That said, they benefit from still supportive global growth and a very healthy US macro and corporate momentum. Furthermore, EU companies exposed to trade show already low multiples (Autos, etc.).

as of 26/11/2024 Index	2024 EPS growth		2025 EPS growth	12m fwd PE	Avg 12m fwd PE since 1995	Avg PEG FY3
S&P500	10%		14%	22.0	16.8	1.3
SPX (median)	7%		10%	19.6	17.5	2.0
Mag. 7 (median)	45%	->	13%	31.1	28.0	1.0
SPX 493 (median)	7%	->	9%	19.5	17.4	2.0
AI Basket 175 (ex. Mag 7)	9%	->	12%	20.0	16.9	1.8
Trump Basket (median)	-3%	->	11%	15.0	14.3	1.7
Dem Basket (median)	8%	->	11%	18.2	16.7	1.7
EU Made in US (median)	6%	->	10%	15.5	17.0	1.6
MSCI EMU	-1%		8%	12.8	14.4	1.6
FTSE 100	0%		6%	11.2	14.0	1.7
MSCI WORLD	7%		12%	19.3	16.4	1.4
Russell 2000	40%		52%	28.4	22.6	0.6

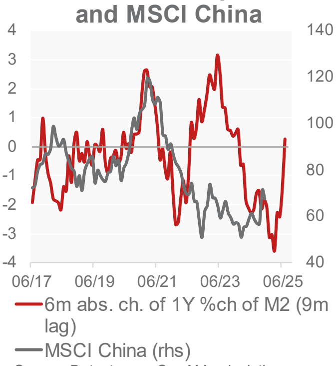
Values for indexes are consensus estimates. Avg PEG FY3 = avg PE using FY3 EPS over 3-5y EPS growth and over FY3-FY0 EPS CAGR. AI Basket 175 is a proprietary basket which includes 175 AI-related companies (60% US, 40% RoW). Source: Datastream, IBES, GenAM

Topix: Price-Book and ROE rel. to US



Source: Datastream, GenAM

China's M2 impulse and MSCI China



Source: Datastream, GenAM calculations

The EMU's higher risk premium over the US (all-time high) may persist short term as investors assess political risk and wait for concrete Trump policies. We see 9-17% TR for EMU and 4-8% for the US in 12 months. EMU should benefit later on from stabilising growth, Chinese stimulus and possible Trump-induced wars' ceasefire. OW EU ex-EMU (lower macro and political risk vs. EMU), OW EU "made in USA", Japan (reforms, valuation, cash yield, positioning and geopolitical risk). OW EU small caps and diversify US into equal-weighted SPX & Russell 2000 (valuation).

EU Sectors: maintain a cyclical tilt given disinflation trend, decent global LDI and ISM momentum ("goldilocks"). Increased Cap. Goods (to N). OW in Construction and RE (lower rates, mortgage demand), Retail, Div. Financials (OW from N), Insurance, A&D (structural EPS revisions), Pharma (good valuation rank and its momentum, EPS revisions gap to price), and Telecoms. Increased UW in Energy, Food and Transportation (both new) and Utilities. Still OW Small vs Large Cap (lower rates, M2 Impulse).

Neutral EM Equities: OW China, India and Malaysia

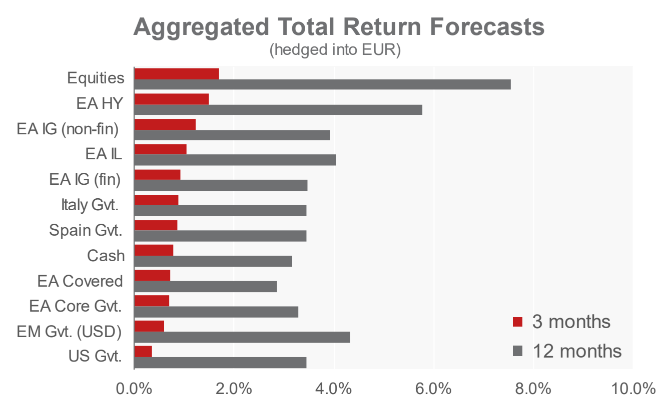
Decreasing sentiment (Sentix), pressure from the strong dollar and possible tariffs represent headwinds for EM. EMs have historically underperformed the DMs after US elections. Still, compared to 2016, EMs macro stability is much better (no external vulnerabilities) and they look much more undervalued vs DM. OW India (lower geopolitical risk, less trade uncertainty, low positioning, structurally high growth), Malaysia (lower geopolitical risk, attractive valuation score) and tactically slightly OW on China, betting on further fiscal stimulus, M2 trend and low valuation.

ASSET ALLOCATION

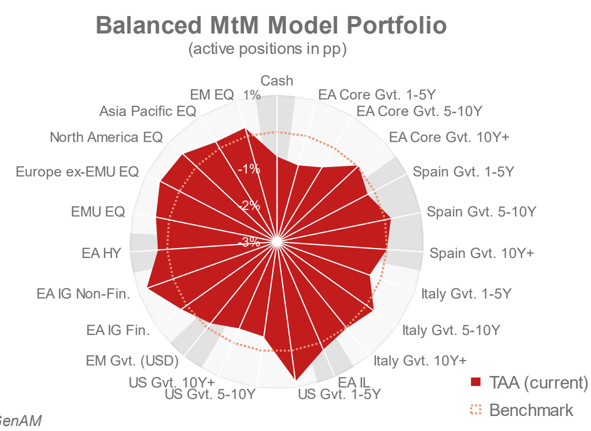
Thorsten Runde

- **Overall, the global economy was well on track in 2024. Above all, US equities were showing a remarkable performance, even completely ignoring the usual set-back in the run-up to the US elections. Clearly preferring Credit over Govies paid out in general while we were too cautious in Equities and HY.**
- **2025 is expected to continue revealing resilient global growth. However, we assume significant regional differences, in particular between the US and the euro area. Regardless of all imponderables related to it, Trump 2.0 will be growth supportive for the former (taxes) and burdensome for the latter (tariffs). Furthermore, the euro area will continue to suffer from the political uncertainties in France and Germany.**
- **For now, we recommend a small overweight in Equities and HY. We continue to favour IG Credit over Government bonds on carry grounds. We prefer non-Financials to Financials given the latter's exposure to French sovereign risk. We underweight Govies in general and go for a small long duration in the euro area on the expectation of modestly lower yields. In the US we prefer the short end of the curve give the inflationary Trump policies.**

Global growth is expected to stay resilient in 2025. However, we anticipate significant regional differences. Already backed by solid consumption and rising real income, tax cuts under Trump 2.0 will add to the US growth outlook. By contrast, the euro area is burdened by the political imponderables in France and Germany and by the trade risks stemming from Trump 2.0. China is seen to continue struggling with its property crisis and weak consumer confidence. Emerging markets' growth is set to lose some momentum given the exposure to US tariffs, slower Chinese growth, and a stronger USD.



Source: GenAM



Source: GenAM

All in, resilient global growth, receding inflation, and rate cuts should continue to underpin risk sentiment. Thus, we moderately overweight Equities and HY Credit. We stay positive on EA IG Credit given its carry and its better risk-reward-ratio compared to non-Core Govies. As France's share in the Financials is particularly high, and thus its exposure to French sovereign risk, we do have a clear preference for the non-Financial sector. We underweight Govies in general. We recommend a small long duration in the euro area with ECB rate cuts, lower inflation, and burdened growth pointing towards lower yields here. In the US we prefer the shorter maturities as a further rise in yields appears likely against the backdrop of the expected economic policy measures under Trump. Given the currently well backed USD strength we moderately overweight the greenback while simultaneously drawing exposure from USD-denominated external EM sovereign debt.

FORECASTS

Macro Data

Growth	2023	2024		2025		2026
		forecast	Δ vs. cons.	forecast	Δ vs. cons.	forecast
US	2.5	2.8	0.1	2.4	0.5	2.5
Euro area	0.5	0.8	0.0	0.8	- 0.3	1.4
Germany	- 0.1	- 0.1	- 0.0	0.3	- 0.3	1.4
France	0.9	1.0	- 0.1	0.5	- 0.4	1.3
Italy	0.9	0.7	0.1	0.6	- 0.2	0.6
Non-EMU	0.2	1.1	0.0	1.4	0.0	1.9
UK	0.1	0.9	0.0	1.3	0.0	1.9
Switzerland	0.8	1.5	0.0	1.4	0.0	1.8
Japan	1.9	- 0.1	0.0	1.2	- 0.0	0.9
Asia ex Japan	5.3	5.1	- 0.0	4.9	0.1	4.6
China	5.2	4.8	- 0.0	4.5	0.0	4.1
CEE	3.1	2.9	- 0.1	2.2	- 0.1	2.3
Latin America	2.1	1.7	0.0	2.1	0.0	2.6
World	**3.2**	**3.2**	**0.0**	**3.1**	**0.1**	**3.1**

Inflation	2023	2024		2025		2026
		forecast	Δ vs. cons.	forecast	Δ vs. cons.	forecast
US	4.1	2.9	- 0.0	2.4	0.1	2.3
Euro area	5.5	2.4	0.0	2.0	0.1	2.0
Germany	6.0	2.4	0.1	2.0	- 0.0	2.0
France	5.7	2.3	0.1	1.7	0.2	2.0
Italy	5.6	1.3	0.2	1.8	0.0	1.8
Non-EMU	6.6	2.4	0.0	2.0	0.0	1.9
UK	7.4	2.6	0.0	2.4	0.0	2.1
Switzerland	2.2	1.4	0.3	0.7	0.0	1.0
Japan	3.3	2.3	- 0.3	2.4	0.3	2.0
Asia ex Japan	2.2	2.0	0.1	2.4	0.3	2.7
China	0.2	0.4	- 0.0	1.3	0.2	2.0
CEE	19.0	19.2	0.2	11.4	0.3	7.4
Latin America	5.1	4.6	0.0	3.8	0.0	3.1
World	**5.1**	**4.0**	**0.1**	**3.2**	**0.2**	**2.9**

Regional and world aggregates revised to 2015 IMF PPP weights; Latin America Inflation excluding Argentina and Venezuela

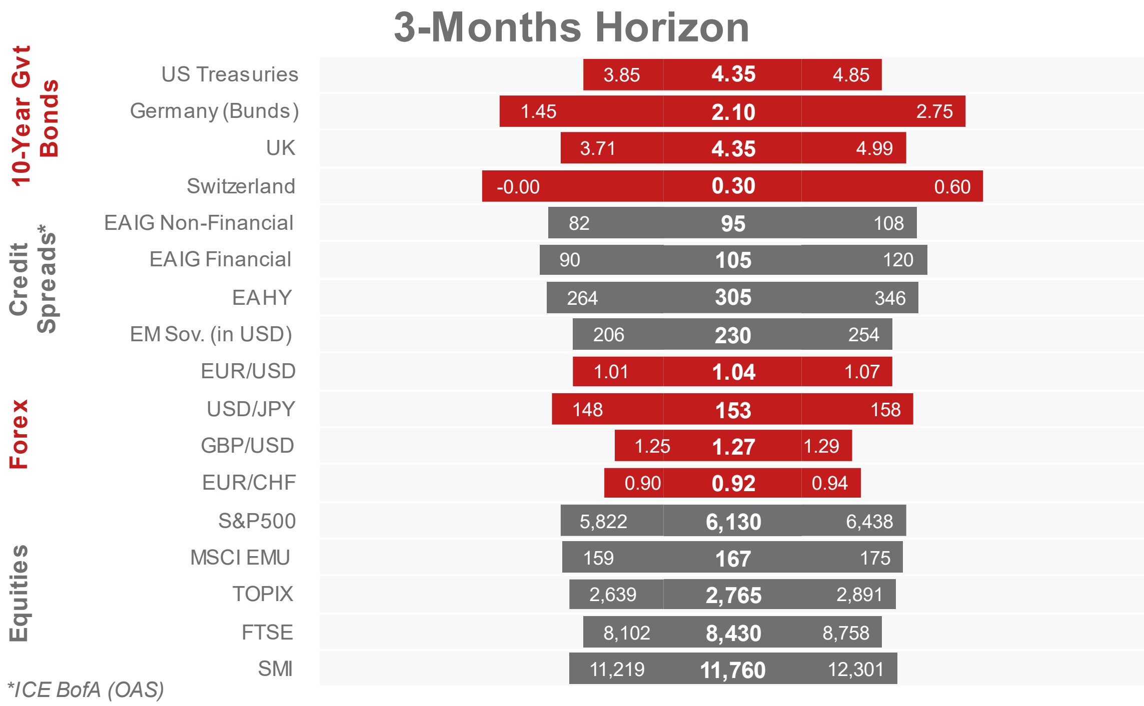
Financial Markets

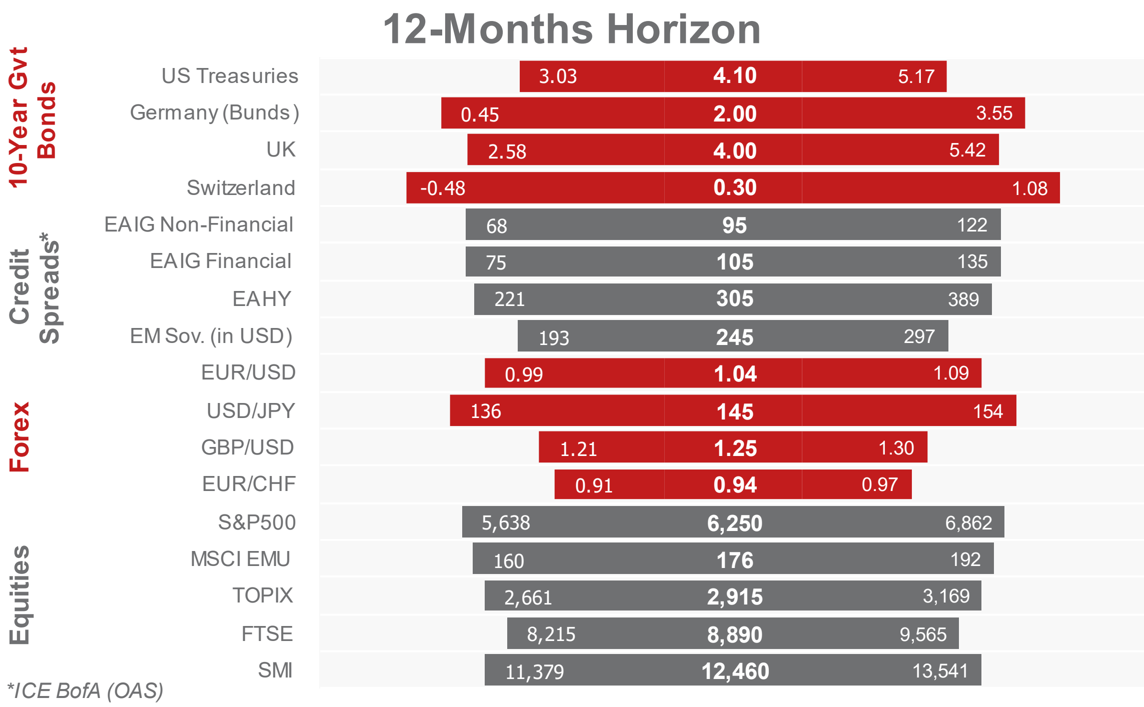
Key Rates	Current*	3M		6M		12M	
		Forecast	*Forward*	*Forecast*	*Forward*	*Forecast*	*Forward*
US (upper bound)	4.75	4.50	*4.18*	4.00	*3.93*	3.75	*3.71*
Euro area	3.25	2.75	*2.26*	2.00	*1.84*	1.75	*1.63*
Japan	0.25	0.50	*0.44*	0.75	*0.54*	0.75	*0.70*
UK	4.75	4.50	*4.44*	4.25	*4.18*	4.00	*3.84*
Switzerland	1.00	0.50	*0.37*	0.25	*0.15*	0.25	*0.04*
10-Year Gvt Bonds							
US Treasuries	4.23	4.35	*4.25*	4.30	*4.26*	4.10	*4.30*
Germany (Bunds)	2.12	2.10	*2.15*	2.05	*2.15*	2.00	*2.19*
Italy	3.20	3.20	*3.24*	3.20	*3.28*	3.25	*3.40*
Spread vs Bunds	*108*	*110*	*109*	*115*	*113*	*125*	*120*
France	2.88	2.90	*2.90*	2.90	*2.93*	2.95	*3.01*
Spread vs Bunds	*76*	*80*	*75*	*85*	*78*	*95*	*82*
Japan	1.06	1.05	*1.13*	1.00	*1.18*	0.95	*1.27*
UK	4.31	4.35	*4.33*	4.25	*4.33*	4.00	*4.36*
Switzerland	0.26	0.30	*0.26*	0.30	*0.26*	0.30	*0.28*

**3-day avg. as of 11/12/24*
***ICE BofA (OAS)*

Credit Spreads**	Current*	3M		6M		12M	
		Forecast	*Forward*	*Forecast*	*Forward*	*Forecast*	*Forward*
EA IG Non-Financial	94	95		95		95	
EA IG Financial	101	105		105		105	
EA HY	305	305		305		305	
EM Sov. (in USD)	221	230		240		245	
Forex							
EUR/USD	1.05	1.04	*1.06*	1.03	*1.06*	1.04	*1.07*
USD/JPY	152	153	*150*	150	*149*	145	*146*
EUR/JPY	160	159	*159*	155	*158*	151	*157*
GBP/USD	1.28	1.27	*1.28*	1.26	*1.27*	1.25	*1.27*
EUR/GBP	0.83	0.82	*0.83*	0.82	*0.83*	0.83	*0.84*
EUR/CHF	0.93	0.92	*0.92*	0.92	*0.92*	0.94	*0.91*
Equities							
S&P500	6,057	6,130		6,170		6,250	
MSCI EMU	165.4	167.0		167.5		176.0	
TOPIX	2,742	2,765		2,780		2,915	
FTSE	8,311	8,430		8,565		8,890	
SMI	11,695	11,760		11,755		12,460	

Forecast Intervals





*The forecast range for the assets is predetermined by their historical volatility. The volatility calculation is based on a 5-year history of percentage changes, equally weighted in the case of the 12-month forecast and exponentially weighted in the case of the three-month forecast. The length of the bars within each asset group is proportional to the relative deviations from their mean forecasts.

IMPRINT

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