*Anima***Insight**

Equity Strategy
BUY WEAK

We reiterate our tactical LONG stance. *Despite the recent volatility, we expect the global benchmark, driven by the US, to recover recent losses and move towards new highs. The resilient macro backdrop, supportive Central Banks, and a likely reversal of the recent upward trend in rates will support equity valuations.*

Regionally, the US remains our preferred market, while the UK is our least favoured. *We continue to maintain a NEUTRAL stance on Europe, Japan, and EM. Specifically:*

1) *In Europe, risks are currently finely balanced. Pros, such as light positioning, depressed valuations, supportive monetary policy, peace talks, and a strong USD are counterbalanced by cons mainly stemming from political uncertainty in France and Trump's tariff rhetoric.*

2) *In Japan, Yen depreciation is losing momentum, but improvements in margins and dividends still support valuations.*

3) *In EM, downward pressures driven by President Trump's rhetoric and the strong USD may be offset by extremely depressed valuations and expectation of support from Chinese authorities, potentially triggering a sharp rally similar to the one in September 2024.*

At the sector level, we stick to our cyclical tilt with a mild preference for Growth/Quality names *(previously barbelled). Globally, we remain LONG on Semiconductors, Software, and Media in the Growth sectors, while Banks and Diversified Financials are our top picks in the Value space. Pharma, Biotech and Life Science are our favourite Defensive sectors (previously SHORT).*

Strategically, we remain OVERWEIGHT. We continue to anticipate a 15% market gain in 2025, *driven by around 10% earnings growth and multiple expansion. Therefore, we view any market dips as buying opportunities.*

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Regionally, we strategically favour the US over the Rest of the World due to a stronger macroeconomic backdrop. *Our baseline for US GDP growth suggests that US EPS will grow by at least 10% in 2025, with a potential additional boost of approximately 4% from the tax reforms proposed by President-Elect Trump.*

We maintain a NEUTRAL stance on Europe, *as we do not expect a likely ceasefire between Russia and Ukraine to be sufficient to trigger a self-sustained rally in continental equities. We view this as a short-lived tactical trade opportunity rather than a structural shift from US exceptionalism. We remain strategically NEUTRAL on EM, as the supportive measures from Chinese authorities still fall short of boosting internal demand, disappointing investors.*

On the sector front, we maintain our strategic tilt towards Growth and Quality, *expecting the so called Magnificent 7 to continue leading the way.*

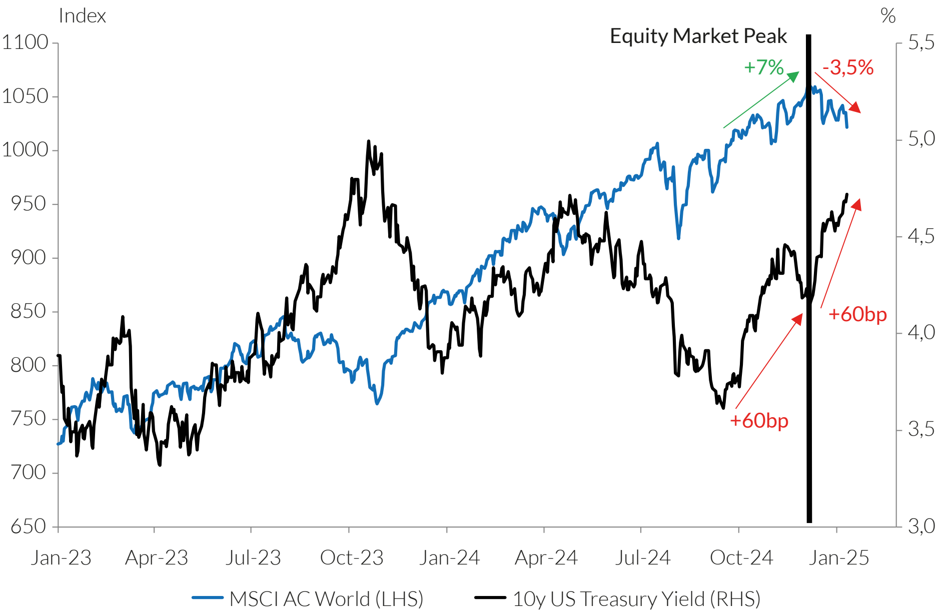
A structural change in our inflation outlook and a reversal of the easing stance of the main Central Banks would prompt us to be more cautious on equities and long-duration sectors. However, this is not our baseline at the moment.

MARKET OVERVIEW: STAY LONG

The global benchmark is now 3.5% below its all-time peak recorded in December 2024. The recent weakness followed a 16% rally from August's lows and coincided with 60bp sell-off in US Treasury. The increase in US Treasury yields began in mid-September: the initial 60 basis points sell-off in US government bonds supported equities, particularly their cyclical components. However, the subsequent 60 basis points rise in yields had a negative effect on the asset class overall (**Figure 1**).

FIGURE 1.

MSCI AC World Index and 10-year US Treasury Yield



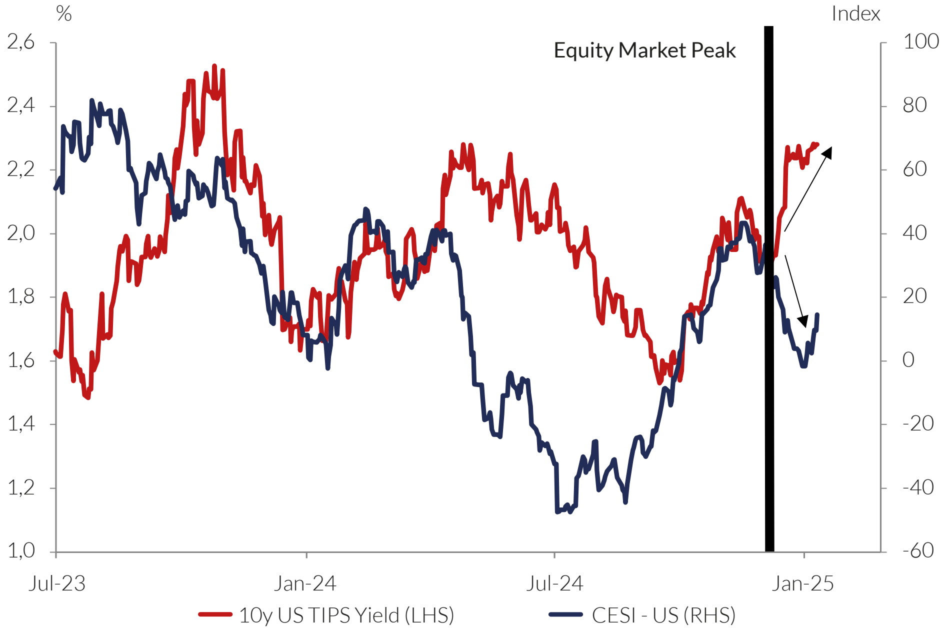
Source: MSCI, ANIMA Research. Note: prices as of 10 January 2025.

We consider the recent movement in nominal yields, driven equally by real yield and breakeven, is not justified by the current macro backdrop. Since early December, the 10-year US TIPS yield has risen by 38bp, breaking its logical relationship with the US Economic Surprise Index (CESI) - the real yield increased while the US CESI declined. In our view, this decoupling is unsustainable. As we do not expect a sharp reacceleration of economic data from this point, **we anticipate real yields to roll over as they did in Q2 last year** (**Figure 2**).

Furthermore, the 10-year US breakeven overshot in Q4 2024, breaking its close relationship with oil prices. The decoupling began in early October, and by the US Election Day, the breakeven had risen by approximately 20bp, while Brent crude oil prices had decreased by 5%. This sharp movement was primarily driven by rising investor concerns about Trump's potentially inflationary policies rather than actual macroeconomic factors. The breakeven continued to rise by 10bp since the start of the year, alongside a 3% increase in oil prices, but the gap between the two variables remains wide and unsustainable (**Figure 3**). Therefore, **we expect the breakeven, which is already trading near the upper bound of its three-year range, to revert**, along with a weakening in oil prices, whose recent increase was mostly due to temporary factors rather than a genuine rise in demand.

FIGURE 2.

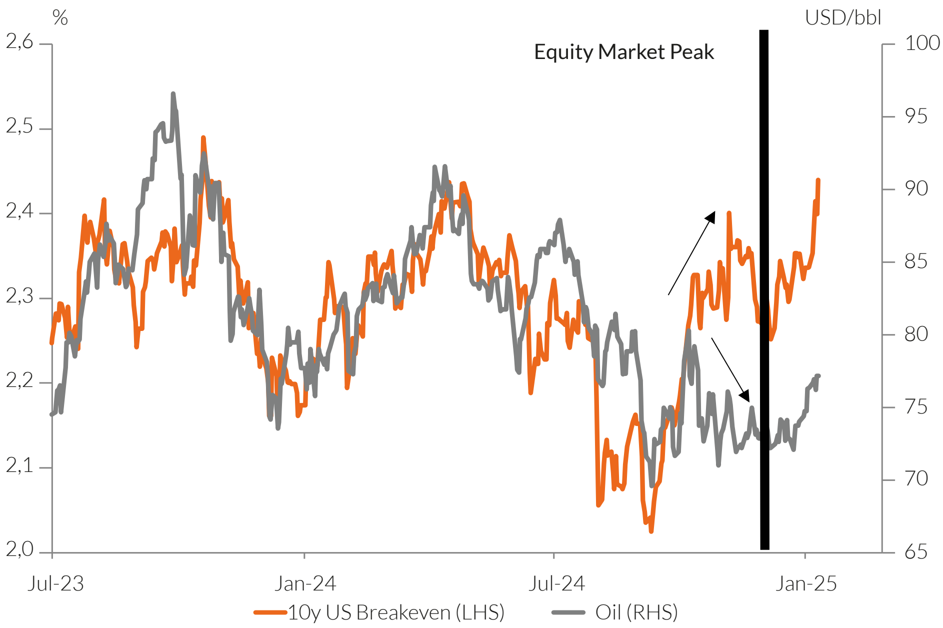
Decoupling I: US Real Yield and US CESI



Source: Citi, Datastream, ANIMA Research. Note: prices as of 10 January 2025.

FIGURE 3.

Decoupling II: US Breakeven and Crude Oil Price



Source: Bloomberg, ANIMA Research. Note: prices as of 10 January 2025.

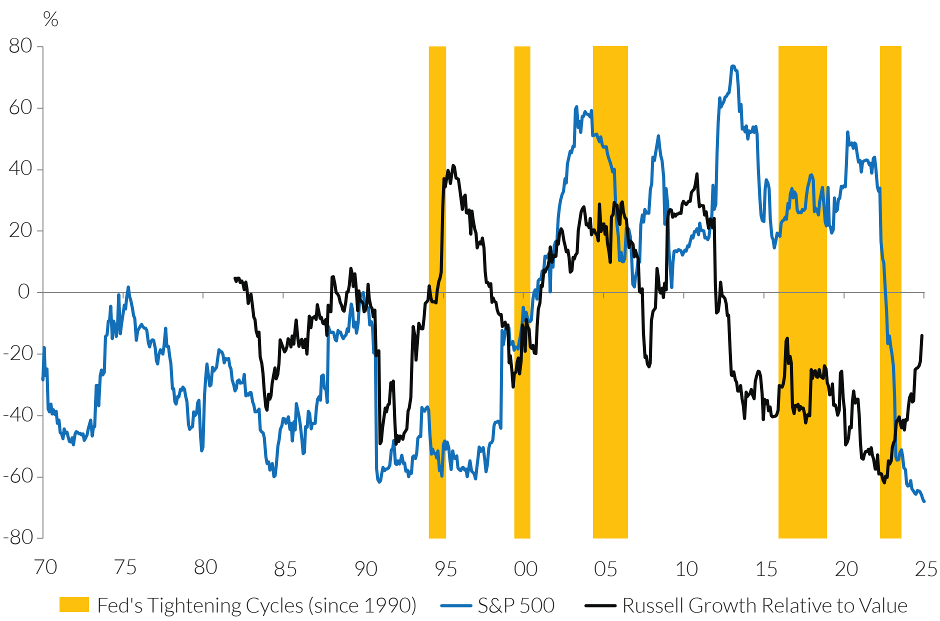
We expect nominal yields to halt their upward trend, decline, and no longer act as a headwind for equities. Notably, since November 2021, and particularly during the Fed's tightening cycle that began in March 2022, the correlation between government yields and US equity performance shifted. It diverged from the positive relationship seen over the previous two decades and returned to the negative correlation observed between 1970 and 1998. Thus, from late '90s to 2022, rising nominal yields were associated with positive equity performance.

However, **over the last couple of years, rising yields have become detrimental to the stock market overall**. Interestingly, during the same period, **nominal yields have become less relevant in explaining Growth versus Value trades**, with correlations dropping from -62% (r^2 40%) to just -10% (r^2 0%), (**Figure 4**). We observe a similar correlation pattern even for global equities, not just in the US.

Given this backdrop, we expect lower bond yields to support stock prices. Therefore, we maintain our LONG position on equities adopted post-US election, viewing the current market volatility as primarily driven by concerns about higher inflation in the US rather than fundamental or macroeconomic factors. In fact, incoming data continue to support a goldilocks narrative for the US economy. Growth remains robust as aggregate labour income supports consumer spending. Meanwhile, inflation continues to adjust downward, albeit slowly and occasionally erratically. We maintain our above-consensus view that the US economy will experience a "soft" soft landing this year.

FIGURE 4.

3-year Rolling Correlations between 10-year US Treasury Yield and US Equities

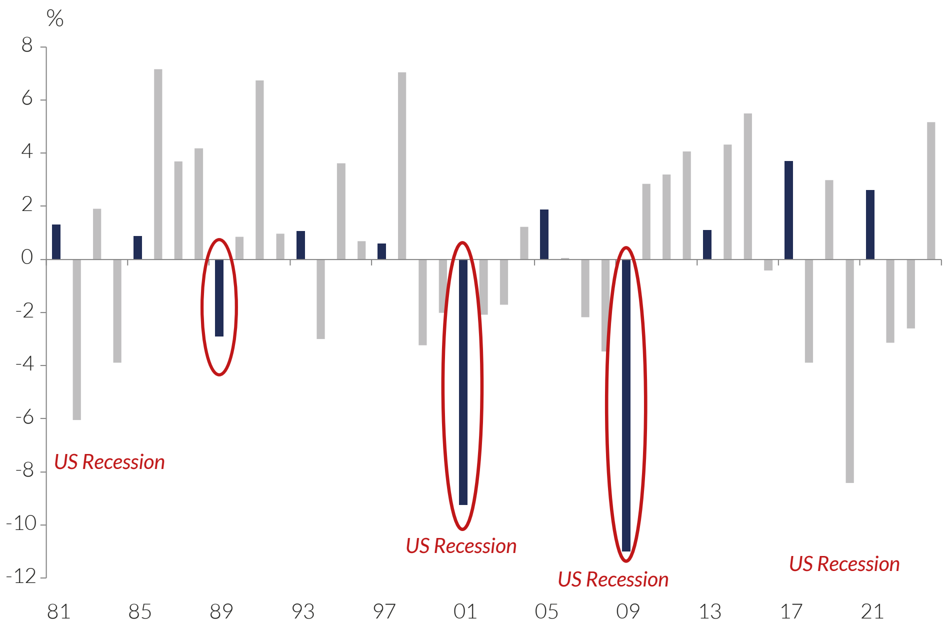


Source: S&P 500, Russell, ANIMA Research. Note: prices as of 10 January 2025.

Seasonality also supports maintaining an engagement with equities. Historically, February of the first year of a new US Presidency tends to be a positive month for the asset class, with a hit ratio above 70%. Exceptions were in 1989, 2001, and 2009. During the latter two periods, the US was in a recession, which is not the case now (**Figure 5**).

FIGURE 5.

S&P 500 performance every February since 1981
(highlighted in blue for US Presidential Inauguration years)



Source: S&P, ANIMA Research.

TACTICAL VIEW

a. Regional Allocation

Regionally, the US remains our preferred market, while the UK is our least favoured. The former market has a Quality tilt (**Figure 6**), benefits from a stronger macro backdrop, and is posting strong earnings and margins momentum (**Figure 7**). The latter, a traditional Value market, is experiencing a decline in its forward EPS (3m EMo -5pp).

We continue to maintain a NEUTRAL stance on Europe, Japan, and EM. Specifically:

1) In Europe, risks are currently finely balanced. Pros, such as light positioning, depressed valuations, supportive monetary policy, peace talks, and a strong USD are counterbalanced by cons mainly stemming from political uncertainty in France and Trump's tariff rhetoric.

2) In Japan, Yen depreciation is losing momentum, but improvements in margins and dividends still support valuations (**Figure 8**).

3) In EM, downward pressures driven by President Trump's rhetoric and the strong USD may be offset by extremely depressed valuations and expectation of support from Chinese authorities, potentially triggering a sharp rally similar to the one in September 2024. Therefore, within the region, we are upgrading Taiwan to LONG (from NEUTRAL) due to its strong fundamentals and Quality tilt, while downgrading China to NEUTRAL (from LONG). China is likely to be the first to face new tariffs from the incoming US Presidency.

FIGURE 6.

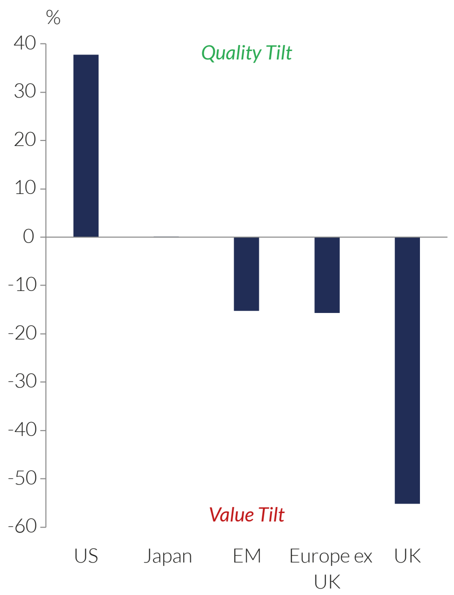
Tactical Regional Recommendations – January 2025

Regional Allocation		
Long	**Neutral**	**Short**
US	EM	UK
	Japan	
	Europe ex UK	
EM Country Allocation		
India	Korea	Brazil
Taiwan	South Africa	Mexico
	China	Indonesia
		Saudi Arabia

Source: ANIMA Research. Note: Markets shown in green have been upgraded, while those in red have been downgraded from the December Strategy Focus.

FIGURE 7.

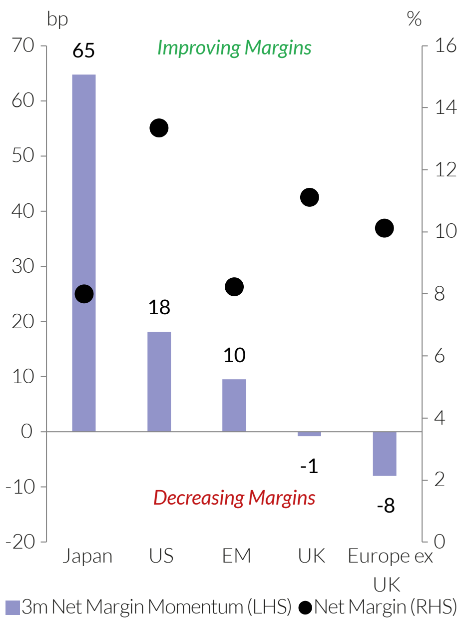
Main Regions: Quality Tilt



Source: MSCI, ANIMA Research.

FIGURE 8.

Main Regions: 3-month Net Margin Momentum



Source: MSCI, ANIMA Research.

b. Sector Allocation

At the sector level, we stick to our cyclical tilt with a mild preference for Growth/Quality names (previously barbelled). Globally, we remain LONG on Semiconductors, Software, and Media in the Growth sectors, while Banks and Diversified Financials are our top picks in the Value space. Pharma, Biotech and Life Science are our favourite Defensive sectors (previously SHORT) due to its high free cash flow yield and strong, improving margins (**Figure 9**).

FIGURE 9.

Tactical Sector Recommendations – January 2025

Industry Group Allocation		
Long	**Neutral**	**Short**
Capital Goods	Tech Hardware & Equip.	Insurance
Semis & Semi Equip.	Commercial & Professional Svcs	Health Care Equip. & Svcs
Media & Entertainment	Retailing	Transportation
Software & Services	Automobiles & Components	Consumer Durables & Apparel
Diversified Financials		Food & Staples Retailing
Banks		Household & Personal Products
Consumer Services		Real Estate
Pharma, Biotech & Life Sciences		Utilities
		Energy
		Materials
		Telecoms

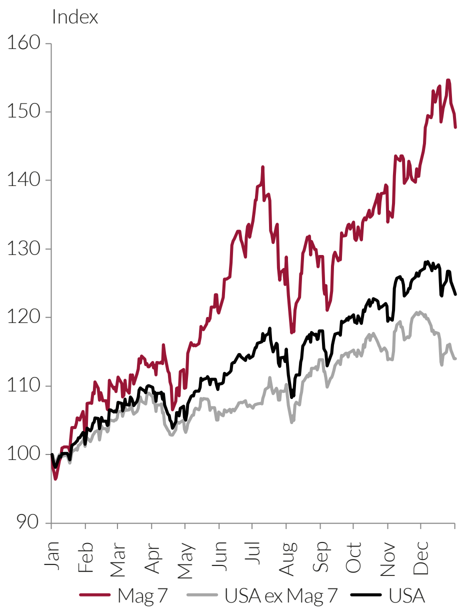
Source: ANIMA Research. Note: Sectors shown in green have been upgraded, while those in red have been downgraded from the November Strategy Focus.

We are focusing on two main themes: the Magnificent 7 and Aerospace & Defence. Our analysis suggests that the Magnificent 7 are strong candidates for market outperformance. Despite their impressive 48% gains last year compared to 14% by others (**Figure 10**), we expect their outperformance to persist and show resilience during volatile market phases. They outperformed the market during the S&P 500 downturns in April, October, and December last year (**Figure 11**). Notably, these Large Caps do not move in unison, but some still offer protection even when they collectively lost money (**Figure 12**). **We expect Magnificent 7's rally to be driven by better fundamentals and a favourable macro environment.** Analysts forecast their aggregate EPS to grow by 20% in 2025, which is 7 percentage points higher than the rest of the market (+13%) (**Figure 13**). The gap is narrowing compared to last year, when the Magnificent 7's EPS grew by 32%, compared to 6% for others. Historically such convergence in earnings growth has not halted the Magnificent 7's outperformance (**Figure 14**).

We recommend increasing exposure to Aerospace & Defence to take advantage of the recent market weakness. The sector, which has outperformed the global benchmark by 11pp per annum since early 2022, offers long-term growth potential, and we believe a ceasefire between Russia and Ukraine will not disrupt this trajectory. After decades of underinvestment, leaving EU forces under-equipped, significant progress is being made in 2024 to close the gap towards NATO's 2% of GDP defence spending target. However, there is still room for improvement, especially if the new US President pushes for an increase to 5% of GDP. As of 2023, 19 out of the 27 EU member states still fell short of the 2% guideline, with Germany, Spain, and Italy facing the largest gaps, needing to increase their defence spending by 20% to 70% of their current levels (**Figure 15**).

FIGURE 10

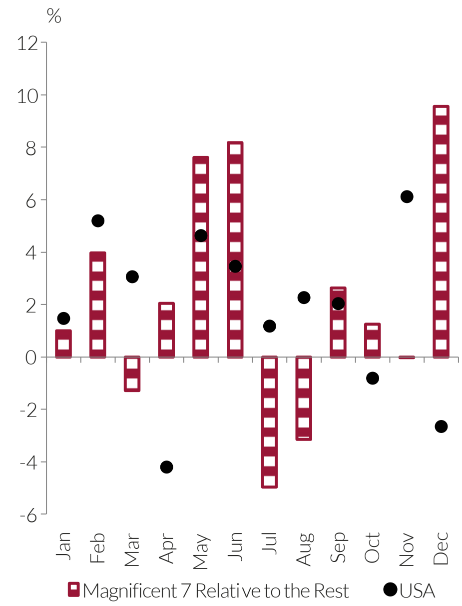
US Equities in 2024



Source: MSCI, ANIMA Research.

FIGURE 11.

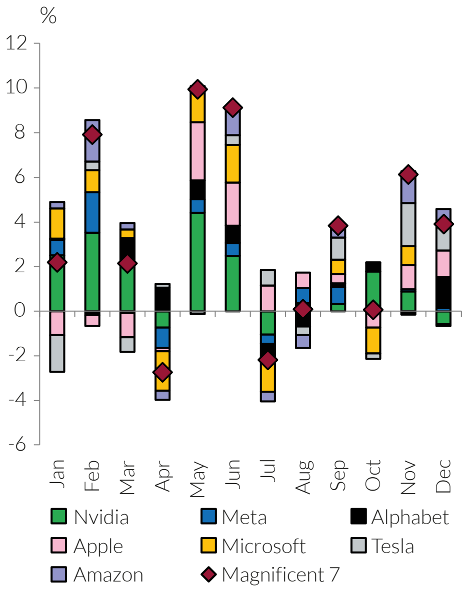
US Equities - Monthly Performance in 2024



Source: MSCI, ANIMA Research.

FIGURE 12

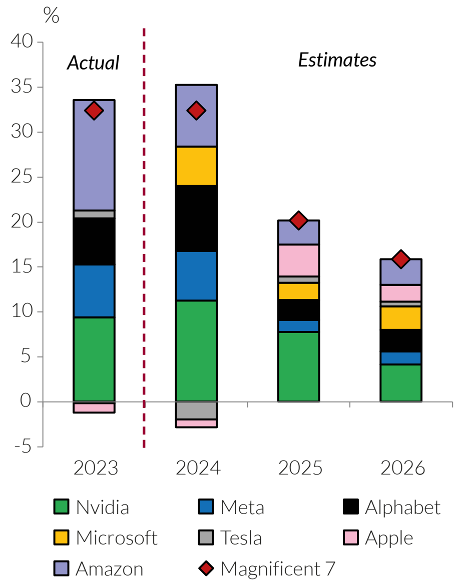
Magnificent 7 - Monthly Performance Decomposition in 2024



Source: MSCI, ANIMA Research.

FIGURE 13.

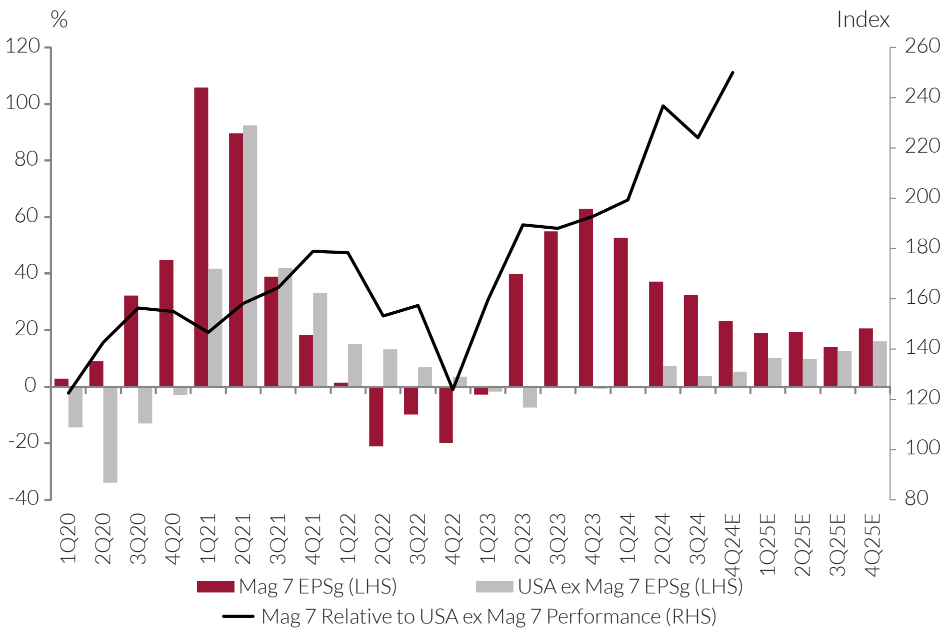
Magnificent 7 – Earnings Growth Rates



Source: Factset, ANIMA Research.

FIGURE 14

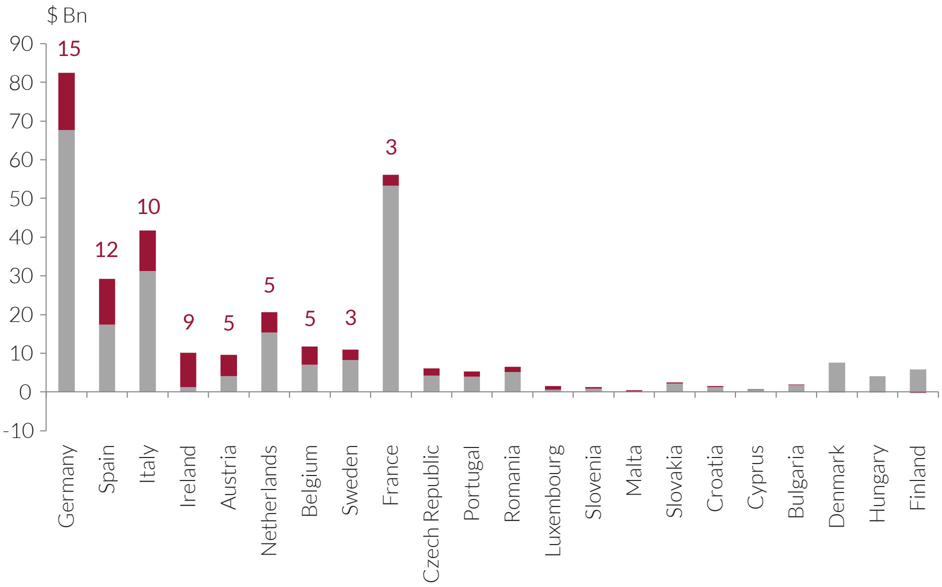
EPS Growth Rate for Magnificent 7 and Rest of Market and Relative Equity Performance



Source: MSCI, ANIMA Research.

FIGURE 15

Defence spending in 2023 – EU Members



Source: European Defense Agency, ANIMA Research.

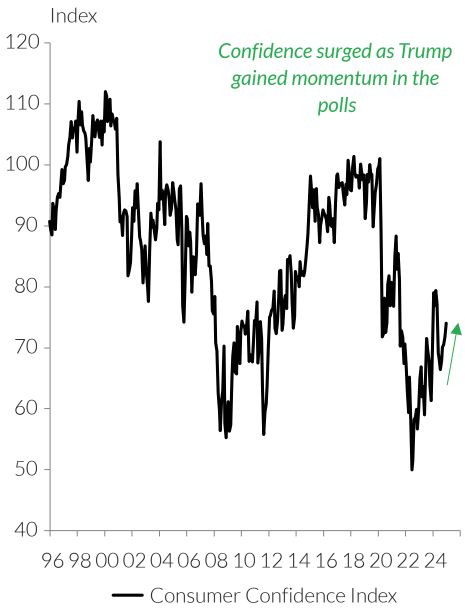
Strategic view: we remain OVERWEIGHT

Strategically, we remain OVERWEIGHT. We still anticipate a 15% market gain in 2025, driven by around 10% earnings growth and multiple expansion. Therefore, we view any market dips as buying opportunities.

From a regional perspective, we strategically favour the US over the Rest of the World due to a stronger macroeconomic backdrop. Our baseline for US GDP growth suggests US EPS will grow at least by 10% in 2025, with a potential additional boost of approximately 4% resulting from the tax reforms proposed by President-Elect Trump. Sentiment indicators for both consumers (demand) and businesses (supply) suggest a positive economic outlook for the next 12 months (**Figure 16** and **Figure 17**).

FIGURE 16.

University of Michigan Consumer Confidence Index



Source: Bloomberg, ANIMA Research.

FIGURE 17.

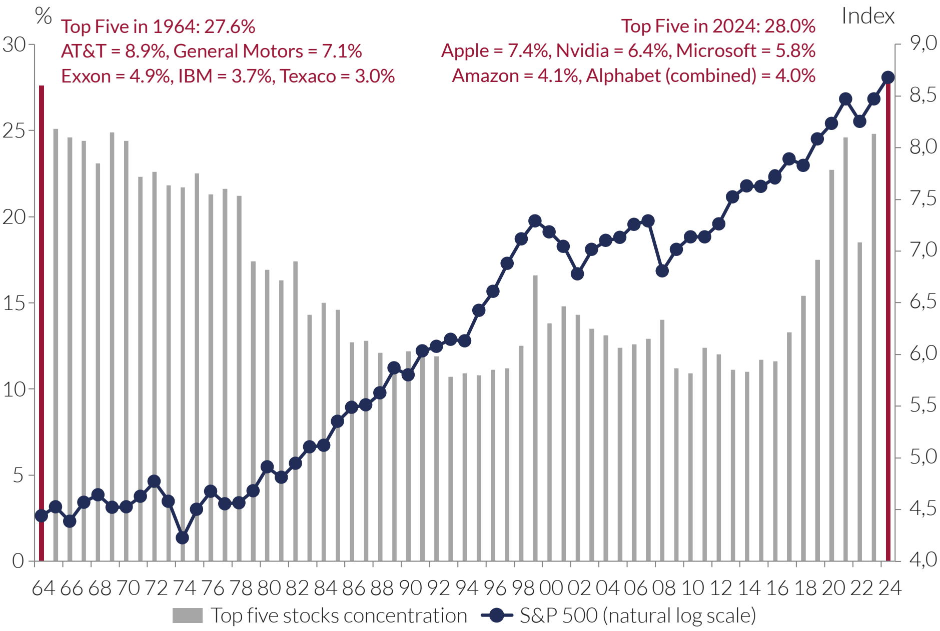
CEO Confidence Index

Source: MSCI, ANIMA Research.

Despite the increasing concentration in the US market, where the largest stocks constitute 28% of the index, we don't view this as a major concern. This level of concentration was last seen in 1964. Although it decreased afterwards, the S&P 500 still gained 9% in 1965, and the top five stocks remained over 20% of the index for 14 years (**Figure 18**). **We believe that changes in equity leadership occur due to significant macroeconomic shifts rather than simple concentration mean reversion.** With no recession expected in the next year, inflation easing, and the Fed in easing mode, we doubt a major de-concentration or leadership change will take place. Historically, previous market churns occurred after the Tech Bubble burst, the GFC, and during the fastest ever Fed tightening cycle of 2022. So, be careful what you wish for.

FIGURE 18.

US Equities' Concentration and S&P 500



Source: S&P, ANIMA Research.

We remain strategically NEUTRAL on Europe, viewing continental equities more as a tactical opportunity than a long-term investment. Even a ceasefire between Russia and Ukraine, anticipated as the baseline for 2025 after Trump's victory, won't be sufficient to trigger a sustained rally in continental equities capable of halting US exceptionalism.

We remain strategically NEUTRAL on EM, as Chinese authorities' supportive measures are still insufficient to boost internal demand, disappointing investors.

From a sector perspective, we continue to maintain our strategic Growth/Quality tilt, anticipating that the so-called Magnificent 7 will continue to lead the way.

APPENDIX

FIGURE 1A.

US Tactical Sector Recommendations – January 2025

Industry Group Allocation		
Long	**Neutral**	**Short**
Media & Entertainment	Commercial & Professional Svcs	Utilities
Software & Services	Tech Hardware & Equip.	Insurance
Semis & Semi Equip.	Retailing	Health Care Equip. & Svcs
Diversified Financials	Transportation	Household & Personal Products
Banks		Food & Staples Retailing
Consumer Services		Food, Beverage & Tobacco
Capital Goods		Real Estate
Automobiles & Components		Telecoms
Pharma, Biotech & Life Sciences		Consumer Durables & Apparel
		Energy
		Materials

Source: ANIMA Research. Note: Sectors shown in green have been upgraded, while those in red have been downgraded from the December 2024 Strategy Focus.

FIGURE 2A.

European Tactical Sector Recommendations – January 2025

Industry Group Allocation		
Long	**Neutral**	**Short**
Software & Services	Health Care Equip. & Svcs	Household & Personal Products
Media & Entertainment	Retailing	Food, Beverage & Tobacco
Food & Staples Retailing	Materials	Tech Hardware & Equip.
Consumer Services	Consumer Durables & Apparel	Real Estate
Capital Goods		Automobiles & Components
Diversified Financials		Energy
Banks		Utilities
Pharma, Biotech & Life Sciences		Transportation
Semis & Semi Equip.		Commercial & Professional Svcs
		Insurance
		Telecoms

Source: ANIMA Research. Note: Sectors shown in green have been upgraded, while those in red have been downgraded from the December 2024 Strategy Focus.

FIGURE 3A.

Industry Group tactical recommendations for the main regions – January 2025

	Global		Regions			
	Sectors	**Industry Groups**	**US**	**Europe**	**Japan**	**EM**
Overweight	Communication Services	Telecoms	-1	-1	1	1
		Media & Entertainment	1	1	0	0
	Financials	Banks	1	1	1	1
		Diversified Financials	1	1	1	0
		Insurance	-1	-1	0	0
	Health Care	Health Care Equip. & Svcs	-1	0	1	0
		Pharma, Biotech & Life Sciences	1	1	1	0
	Industrials	Capital Goods	1	1	0	0
		Commercial & Professional Svcs	0	-1	1	-1
		Transportation	0	-1	0	0
	IT	Software & Services	1	1	0	1
		Tech Hardware & Equip.	0	-1	0	0
		Semis & Semi Equip.	1	1	1	1
Netural	Consumer Discretionary	Automobiles & Components	1	-1	0	0
		Consumer Durables & Apparel	-1	0	0	0
		Consumer Services	1	1	0	0
		Retailing	0	0	-1	-1
	Utilities	Utilities	-1	-1	-1	0
	Energy	Energy	-1	-1	-1	-1
	Materials	Materials	-1	0	0	0
	Real Estate	Real Estate	-1	-1	-1	1
	Consumer Staples	Food & Staples Retailing	-1	1	0	-1
		Food, Beverage & Tobacco	-1	-1	-1	1
		Household & Personal Products	-1	-1	-1	-1

Source: GICS, MSCI, ANIMA Research Note: 1 = Overweight, 0 = Neutral, -1 = Underweight

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