Macro Pulse

The bull-bear battles of 2025

January 2025

Global Market Strategy

At New York Life Investments

Our team of market strategists connects macroeconomics to asset allocation. Leveraging proprietary research alongside the breadth and depth of the New York Life Investments platform, we provide actionable insight into market-driving events, structural themes, and portfolio construction to empower investment decision-making.

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Executive summary

We have lost count of how many years "unprecedented uncertainty" has led annual outlooks, and yet here we are again. It's true that a slower interest rate transition – at least in the United States – rampant global policy uncertainty, and high valuations create challenges for investment strategy. But let's focus on the through lines. Global interest rates are moving lower, unlocking credit growth in public and private markets. A changing global economic landscape requires capital-intensive investment across asset classes and geographies. Higher inflation and interest rates, and higher volatility, have become more likely, such that central banks may once again re-consider the balance between their key goals and long-term needs. Taken at face value, this is an environment that is highly constructive for investor opportunity but may require **significant portfolio change**.

For the last two years, the U.S. economy has defied gravity, providing above-trend economic growth. Though pandemic-era policy programs are fading, other forms of support – including a consistent pro-cyclical fiscal impulse, looser market financial conditions, and a powerful wealth effect – have fostered a soft landing. Cracks have emerged, particularly among lower-income households and lower-quality floating-rate borrowers, but aggregate results are solid.

Our base case scenario is that economic growth slows to near or just below trend over the course of 2025. But a few powerful factors – a decisive "red sweep" in the U.S. election, higher market rates, and persistently painful shelter prices – make it likely that inflation and interest rates are higher and more volatile than historical periods of "average" growth.

This means that the next few quarters are likely to be a balancing act between a slowing economic impulse and sticky data that keep the Fed from providing outright stimulus.

As long as employment and earnings remain resilient, we believe the equity market has room to run. That run, however, may feel more like a trudge; we expect modest gains and sustained volatility compared to the last few years' outsized returns.

That said, **central bank cuts create a meaningful turning point for investment strategy across public and private assets**. Where high interest rates once created income generation opportunity, falling rates make it essential, in our view, to take steps to preserve income. This report lays out strategies for capturing potential equity and real asset opportunities that may emerge from a gradual yield curve normalization.

Outside of the U.S., many countries are coping with the impact of tighter monetary policy: growth is slowing. Many central banks have begun removing their restrictive monetary policy stance, with the Bank of Japan (BOJ) an important exception. Vital for global asset allocation is the direction of the dollar. As U.S. growth is outperforming other developed countries, we expect dollar strength ahead.

This piece is designed to share our holistic global economic, geopolitical, and asset allocation views. Use the links on the table of contents page to explore.

How to invest our macro views

The bull-bear battles of 2025

	Fed Funds rate falling, but slower than before	Market rates likely to be higher and volatile	New policy creates new winners & losers	Persistent capital markets themes
Our view	Deploy cash to counter reinvestment risk	Tactical buying opportunities Cautious on duration	Fade partisanship Follow the fundamentals	Investors can participate in a durable set of a-cyclical investment anchors
How to invest it	Deploy cash into: Short duration credit (i.e. quality high yield, municipal bonds) High-quality leveraged loans This major market turning point creates an attractive, if narrow, window for allocating into private equity, credit, and real estate, in our view.	Yield curve volatility is likely to create tactical bond buying opportunities throughout the coming 6 months Yields may not have peaked: Upward-sloping municipal bond curves remain our preferred spot to add duration	Quality is king Large cap value offers a compelling earnings-valuation dynamic Magnificent 7 offer greater earnings quality than large cap growth as a whole Small cap upside is tactical We still like bipartisan sectors: defense, energy, infrastructure	Long-term investment waves: Energy independence Supply chain reshoring Digital infrastructure Broadening of the AI thesis Private markets expansion Accounting for geopolitical risk

Opinions of New York Life Investments Global Market Strategy, January 2025.

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1 U.S. economic & market outlook

What's next for the U.S. economic cycle?

- Fed policy
- Our economic base case
- Policy impacts of the new administration
- Recession risk
- Structural themes

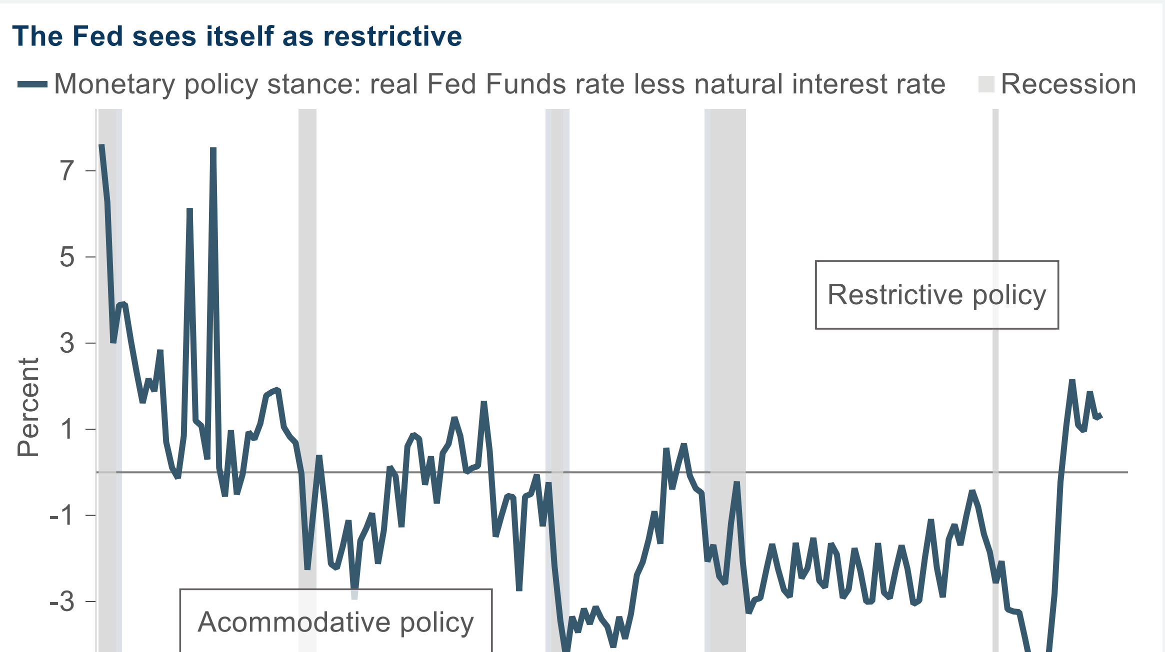
Fed interest rate cuts are likely to extend the economic cycle…

Despite everything, the Fed is cutting back to neutral, removing an important constraint on the U.S. economy

- It is only in the last few quarters that the U.S. economy's total monetary policy stance – the policy rate, less inflation and the natural or "steady state" level of interest in the economy – turned restrictive (**left chart**). Now, the Fed's rate cuts should chip away at, though not immediately reverse, this restrictive stance.

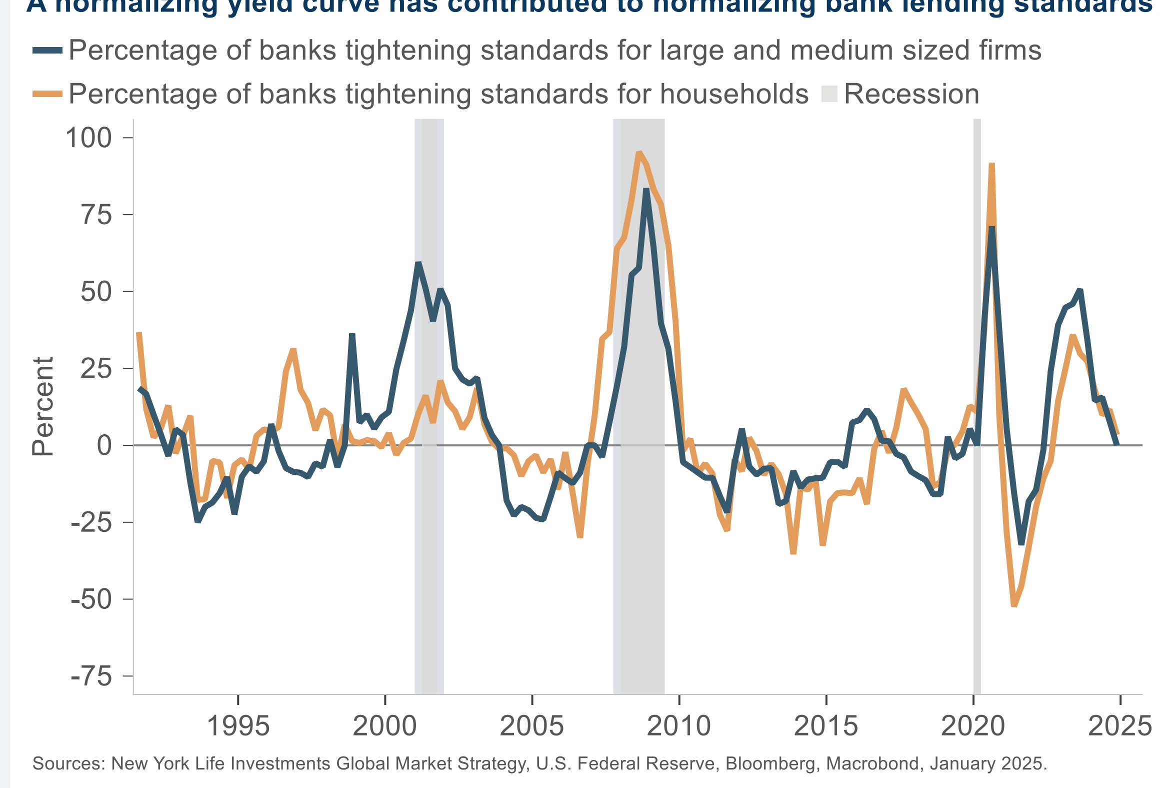
- Lower policy rates have contributed to yield curve normalization and an improvement in bank lending standards (**right chart**). But banks rely on additional factors to influence lending decisions: the regulatory impulse, macroeconomic clarity, and loan demand. It is not clear that loan growth will reaccelerate quickly.

The Fed sees itself as restrictive



Sources: New York Life Investments Global Market Strategy, Federal Reserve, Federal Reserve Bank of Cleveland, Federal Reserve Bank of New York, NBER (National Bureau of Economic Research), Macrobond, January 2025.

A normalizing yield curve has contributed to normalizing bank lending standards



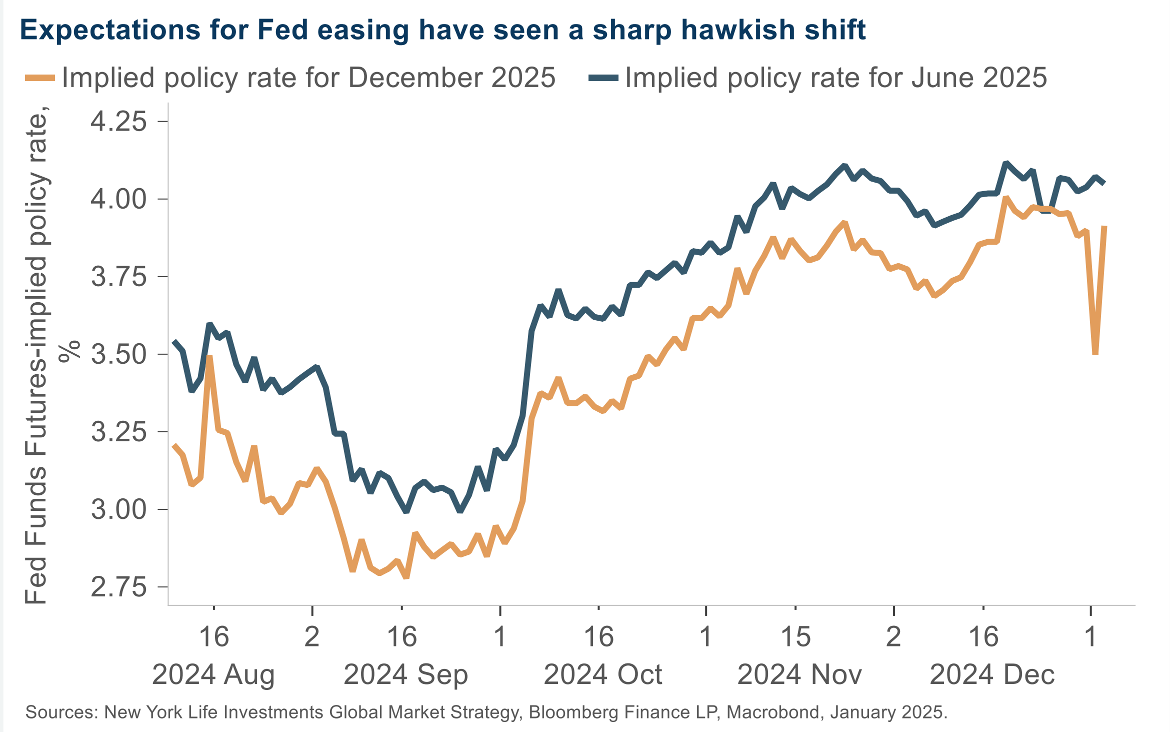
Sources: New York Life Investments Global Market Strategy, U.S. Federal Reserve, Bloomberg, Macrobond, January 2025.

…but the Fed is not easing as fast, or as much, as initially expected

A stronger-than-expected economy has prompted a re-set of expectations for this easing cycle

- The 2024 easing cycle had a strong start, with the Fed electing for a September cut of 50bps rather than 25bps. This unexpected shift encouraged dovish easing expectations; in September, consensus expected Fed Funds to reach 3.0% by mid-2025 (**left chart**).
- Since then, stronger than expected economic activity and election related animal spirits have driven a 100bp hawkish shift in easing expectations. Not only has the pace of expected easing slowed; it is no longer expected that the Fed will reach a neutral interest rate in 2025.
- What is the neutral policy interest rate that neither constraints nor stimulates the economy? Our best estimate is around 3.0-3.5% in nominal terms.
- Upside risks remain for the Fed's path back to neutral, particularly because the Fed's success in controlling inflation is tenuous (**right chart**). Inflation has been in a downward trend, but if easing financial conditions or policies from the new administration support economic activity, inflation may re-firm, slowing the Fed's pace of cuts.

Expectations for Fed easing have seen a sharp hawkish shift



Sources: New York Life Investments Global Market Strategy, Bloomberg Finance LP, Macrobond, January 2025.

Our Fed cuts checklist: conditions met, but we are sleeping with one eye open

Condition	Status	Met?
Inflation expectations well anchored	Long-term inflation expectations remain well anchored.	✓
Core inflation moving closer to target	Core inflation is still above the Fed's target but has made significant progress over the last year. Upside risks to growth may re-firm inflation, which would slow the Fed's pace of cuts all else equal.	✓
Unemployment rate ≥ 4.0%	The unemployment sits around 4.0%, and the Fed has said that it does not want employment to weaken more.	✓
Wage growth commensurate with stable prices	Wage growth is higher than the 3.5% year-on-year figure that we believe would make the Fed comfortable with maintaining a rate cutting cycle. Stickiness in wages may require a slower pace of rate cuts.	✓

Opinions of New York Life Investments Global Market Strategy, January 2025.

The result: a steady macro outlook, but no re-acceleration from here (1/3)

In the best case historical easing cycles, Fed cuts have allowed for stable job creation – but not acceleration

Recession or not, payrolls have never accelerated in an easing cycle

Payroll creation in 12 months pre and post first Fed hike of cycle

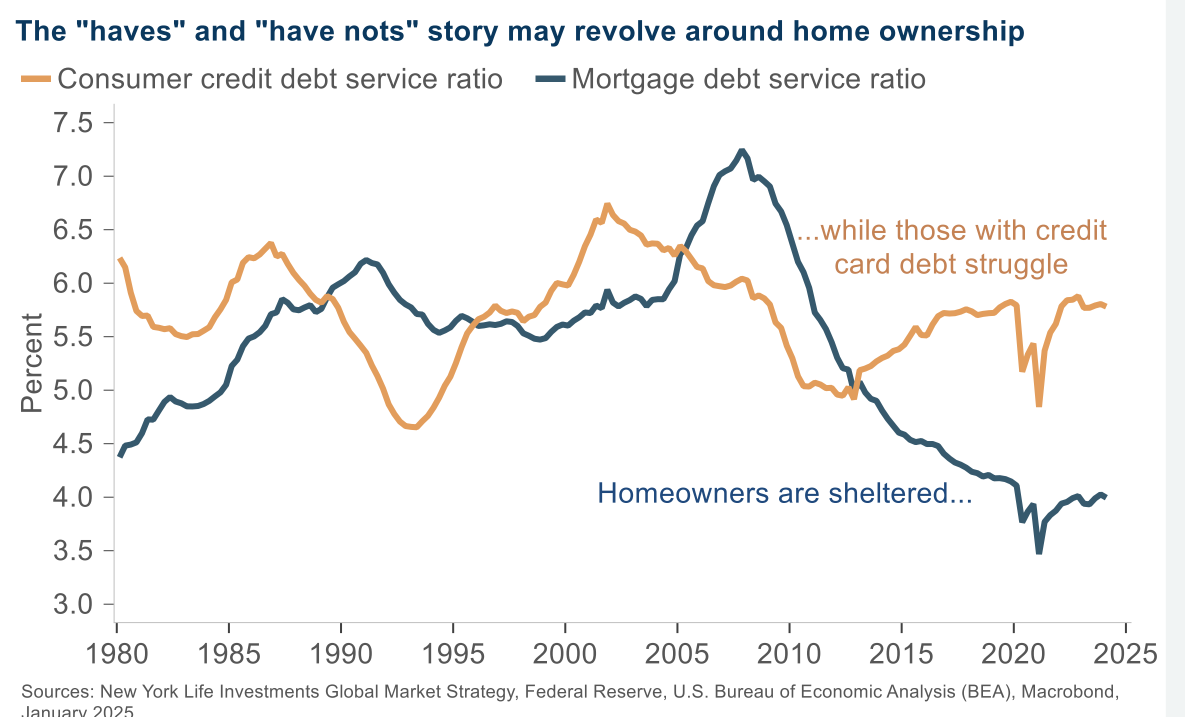
Sources: New York Life Investments Global Market Strategy, U.S. Bureau of Labor Statistics (BLS), Macrobond, January 2025.

TAKEAWAY: Interest rate cuts do not prompt a reacceleration of job creation. At best, the current easing cycle may allow the labor market to stay firm, likely fostering stability for consumers by extension. Labor market stability is paramount to our economic view; strong wages and job availability have carried consumers through an inflationary environment. Major threats to employment or a new wave of hiring can be catalysts for consumer behavior, and therefore for corporate activity.

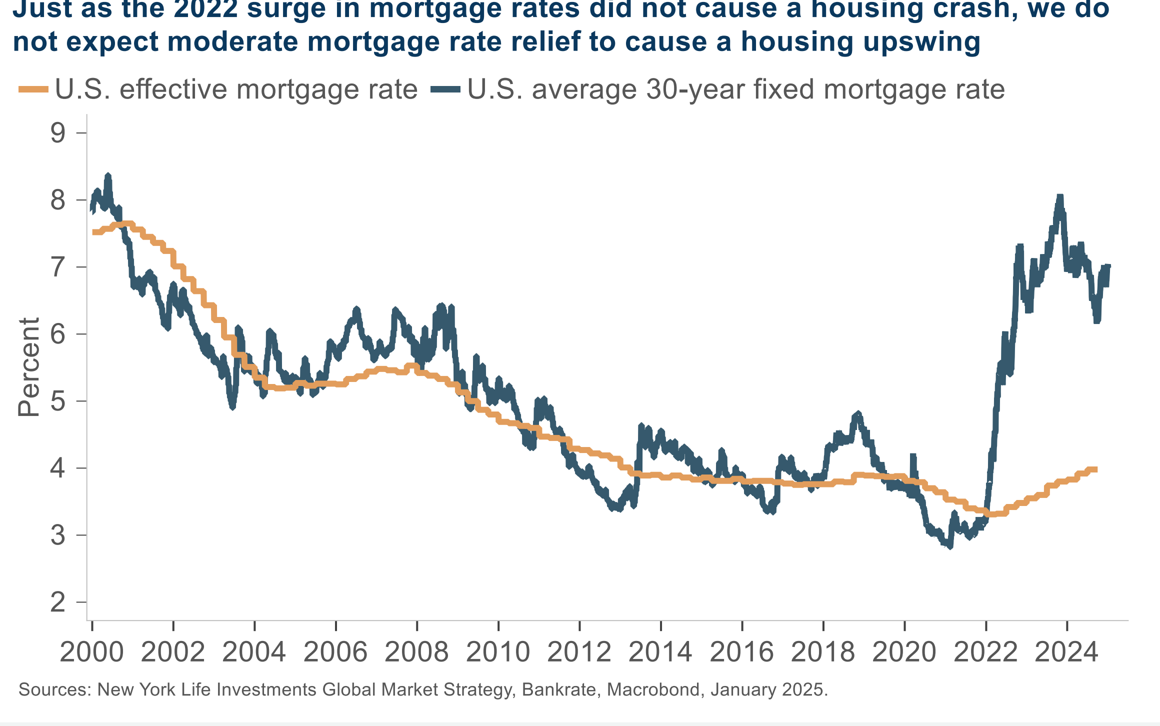
The result: a steady macro outlook, but no re-acceleration from here (2/3)

U.S. consumers remain bifurcated, with housing affordability a key driver of the wedge between segments

- U.S. homeowners have been almost entirely shielded from the Fed's hiking cycle. Mortgage debt service is at the lowest level on record (**left chart**) and homeowners' equity is at the highest level on record. This positive wealth effect has supported higher-income household consumption, seen in rising credit card balances (without rising default rates). In contrast, younger and lower income consumers are seeing rising default rates on credit cards.
- In a departure from the GFC, 90% of mortgages in the U.S. are now fixed rate, meaning that even large swings in mortgage rates are slow to have a systemic effect on housing demand (**right chart**). We are therefore cautious that interest rate relief – particularly in the coming 6 months as the Fed works toward neutral – are a catalyst for higher home prices or accelerated housing investment.
- Barring a shock to housing, hiring, or financial conditions, we expect two-speed consumption to continue.



Sources: New York Life Investments Global Market Strategy, Federal Reserve, U.S. Bureau of Economic Analysis (BEA), Macrobond, January 2025.



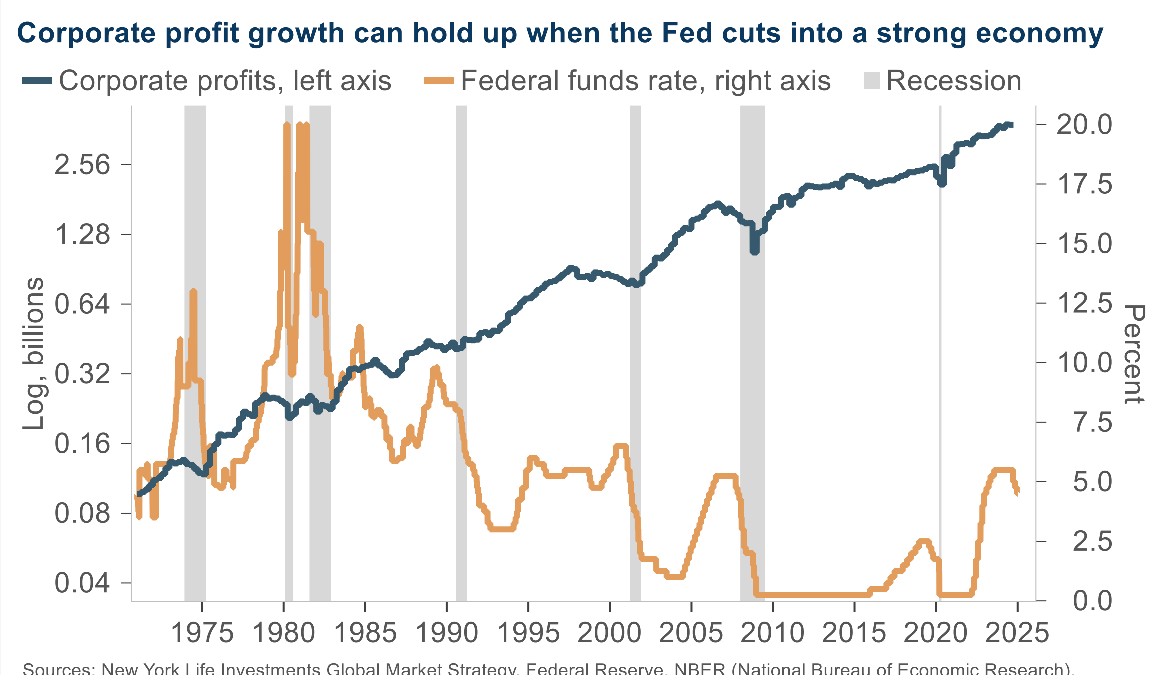
Sources: New York Life Investments Global Market Strategy, Bankrate, Macrobond, January 2025.

The result: a steady macro outlook, but no re-acceleration from here (3/3)

Corporate profits and earnings typically decline during recessions, but absent an economic contraction, historical experience points to resilience

- Corporate profits are primarily driven by the business cycle and are less directly impacted by interest rate cuts from the Fed (**left chart**). Put differently: whether corporate profits hold up as rates move lower depends on what is motivating the policy change. If the Fed is cutting due to recessionary conditions, profits tend to trend lower even amid rate cuts. If the Fed is cutting to normalize the rate environment, corporate profits tend to benefit from economic resilience.
- Companies have been maintaining healthy margins. Today, S&P 500 operating margins are hovering near 13.7%, still above the level of around 12.5% where falling margins have historically become a concern (**right chart**). Technology-driven productivity improvements could support margin expansion in the medium term, but we believe declining consumer spending and sticky labor costs are likely to dominate the near-term story.
- Overall, we expect corporate profits to remain stable – a positive – but are unlikely to meaningfully reaccelerate until the broader economy does.

Corporate profit growth can hold up when the Fed cuts into a strong economy



Sources: New York Life Investments Global Market Strategy, Federal Reserve, NBER (National Bureau of Economic Research), Macrobond, January 2025.

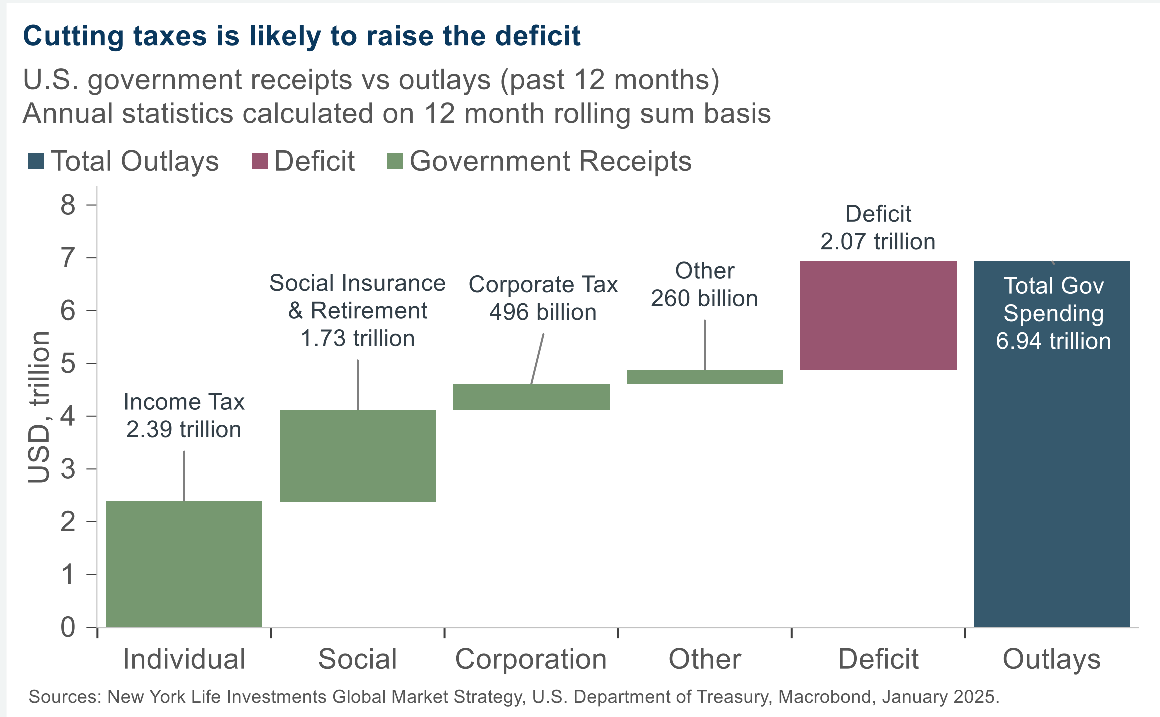
Despite slowing growth and high interest rates, companies have been maintaining stable margins

Sources: New York Life Investments Global Market Strategy, NBER (National Bureau of Economic Research), Bloomberg, Macrobond, January 2025. The S&P 500 Index is an unmanaged index that is widely regarded as the standard for measuring large-cap U.S. stock market performance. Past performance is not a guarantee of future results. It is not possible to invest in an index.

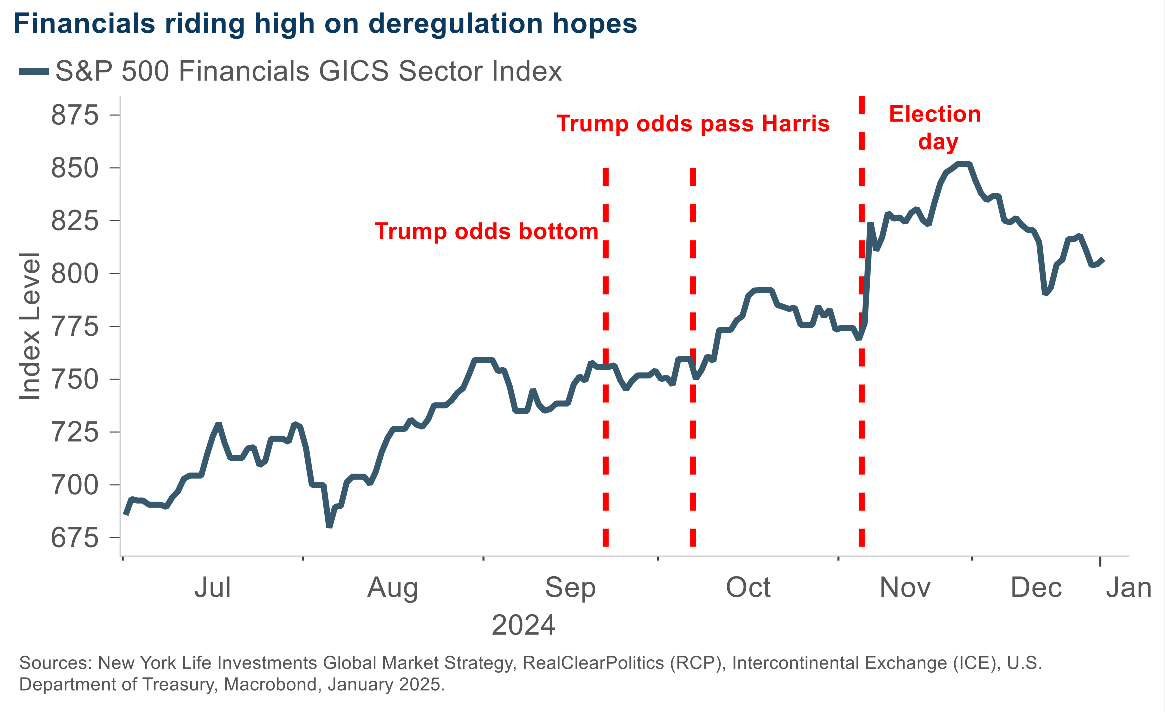
What impact will the new administration have? (1/2)

The exact path of policy is unknowable, but leans inflationary: fiscal policy and de-regulation

- Trump campaigned on extending the 2017 Tax Cuts and Jobs Act, specifically the income tax rate cuts. Lower government revenue will increase the deficit, all else equal (**left chart**).
- Lawmakers – and the rates markets – have started to raise concerns about the growing deficit. The "red sweep" election result makes it unlikely that politics impede deficit spending, but the market could. A higher term premium – reflecting concerns about higher Treasury supply or lower demand – could push market interest rates higher.
- The market has also started in pricing in the potential deregulatory impact of the new administration. For example, the financials sector appeared to be moving higher with Trump's reelection prospects (**right chart**).
- Before riding this wave, we suggest investors balance potential policy impacts against underlying investment drivers: de-regulation can only help so much; macroeconomic factors (improving bank lending standards, steeper curve) help more.



Sources: New York Life Investments Global Market Strategy, U.S. Department of Treasury, Macrobond, January 2025.



Sources: New York Life Investments Global Market Strategy, RealClearPolitics (RCP), Intercontinental Exchange (ICE), U.S. Department of Treasury, Macrobond, January 2025.

What impact will the new administration have? (2/2)

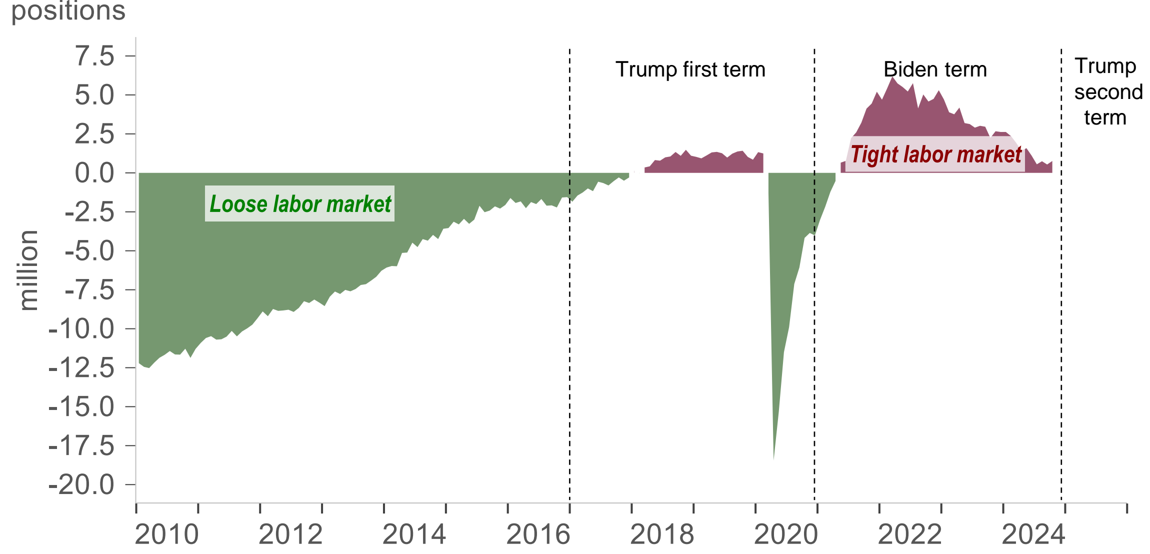
The exact path of policy is unknowable, but leans inflationary: immigration and trade

- At face value, President-elect Trump's stance on immigration is not much different heading into his second term than was true for its first…but the market is. Trump first entered office facing a looser labor market. Entering office in 2025, the labor market has come off its peak growth rates but remains tight (**left chart**). Negative labor supply shocks tend to slow business activity and increase labor costs. At the same time, fewer people in a community results in lower spending and tax receipts, reducing growth.

- The extent of new tariffs is unknowable; U.S. trade partners have significant leverage over the U.S. economy in some cases. But on aggregate, tariffs are almost certainly moving higher. Tariffs are likely to raise consumer prices as they increase the price of imported goods.
- Trump's trade goal is to reduce trade deficits, targeting countries with the largest goods trade surplus to the U.S. (**right chart**). Investors should be mindful of companies or supply chains with exposure to countries such as China, Mexico, Japan, Canada, and those in the EU.

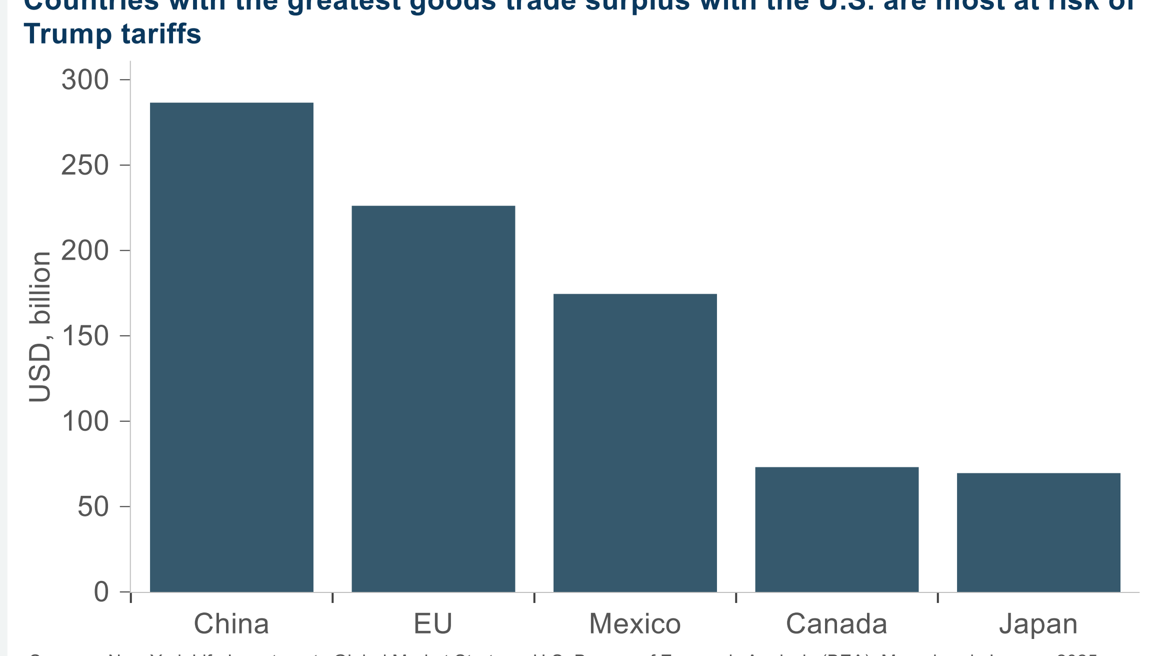
Restrictive immigration policies may have greater impact in a tight labor market

Difference between the labor force and the sum of persons employed and open positions



Sources: New York Life Investments Global Market Strategy, U.S. Bureau of Labor Statistics (BLS), NBER (National Bureau of Economic Research), Macrobond, January 2025.

Countries with the greatest goods trade surplus with the U.S. are most at risk of Trump tariffs



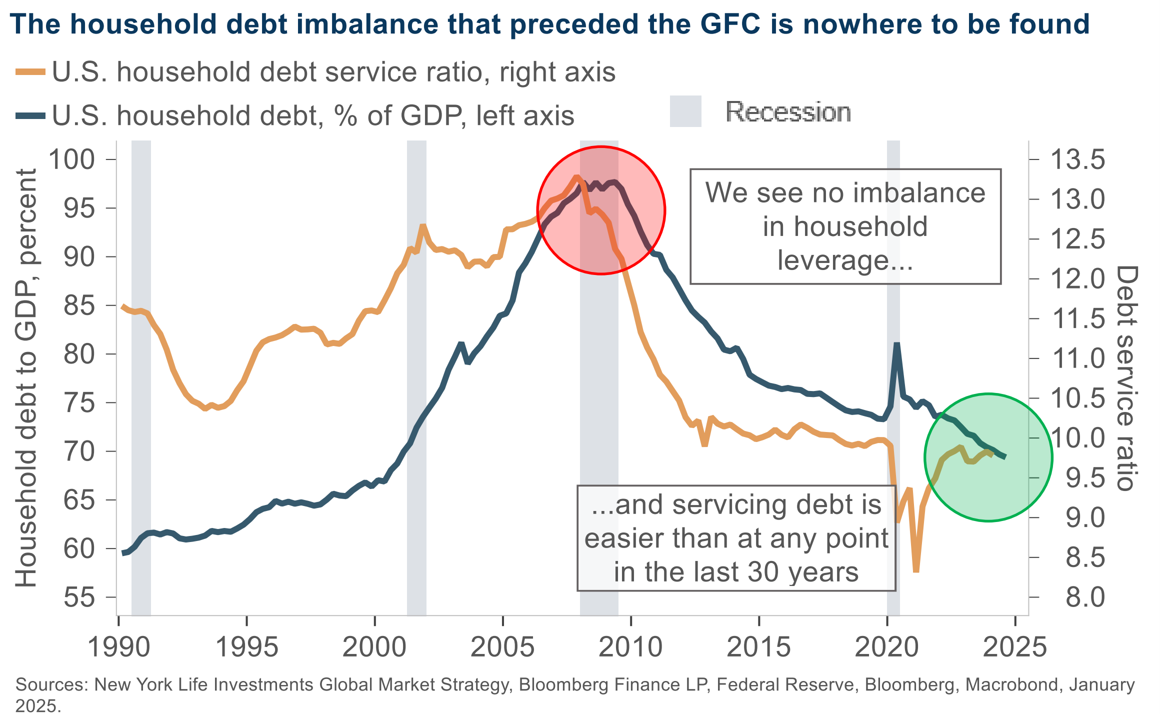
Sources: New York Life Investments Global Market Strategy, U.S. Bureau of Economic Analysis (BEA), Macrobond, January 2025.

Consumers and households are well positioned to weather uncertainty…

Debt imbalances that prompted severe recessions past are not present

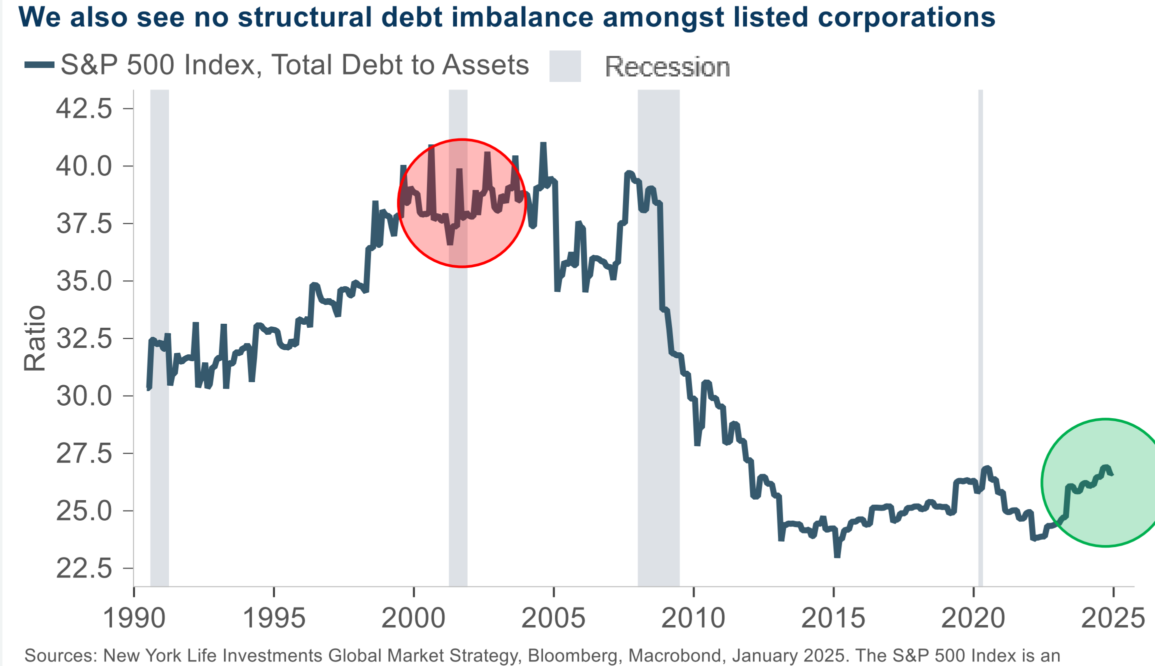
- Overleverage is a commonly recognized crisis trigger point, requiring deleveraging cycles that have made recessions more severe and caused recoveries to lag. Notable recent examples include the GFC's household leverage trigger (**left chart**) and the 2001 recession's corporate leverage trigger (**right chart**).
- Leverage imbalances are not present today, improving the chances of no recession or a mild recession, rather than a financial crisis.
- Lower leverage makes it less likely that an economic shock would cause a pronounced recession – a clear positive for investment probabilities in 2025, in our view. However cracks are beginning to appear among lower income households and lower quality corporate borrowers. An extended economic cycle makes that buildup in leverage more likely in the medium term – something we'll be watching closely.

The household debt imbalance that preceded the GFC is nowhere to be found



Sources: New York Life Investments Global Market Strategy, Bloomberg Finance LP, Federal Reserve, Bloomberg, Macrobond, January 2025.

We also see no structural debt imbalance amongst listed corporations

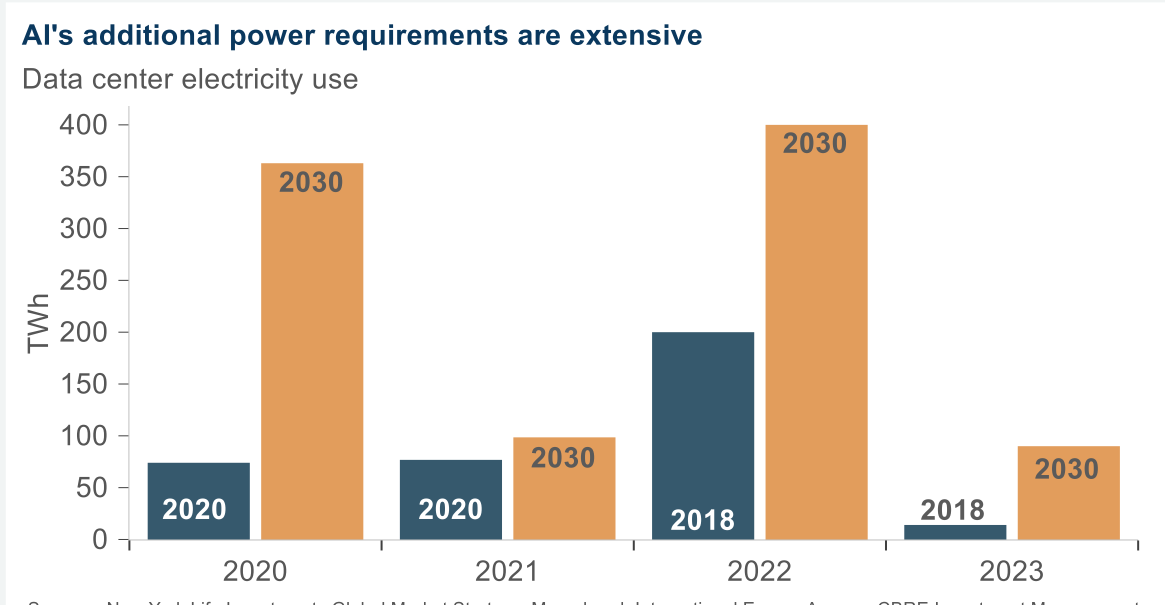


Sources: New York Life Investments Global Market Strategy, Bloomberg, Macrobond, January 2025. The S&P 500 Index is an unmanaged index that is widely regarded as the standard for measuring large-cap U.S. stock market performance. It is not possible to invest in an index. Past performance is not a guarantee of future results.

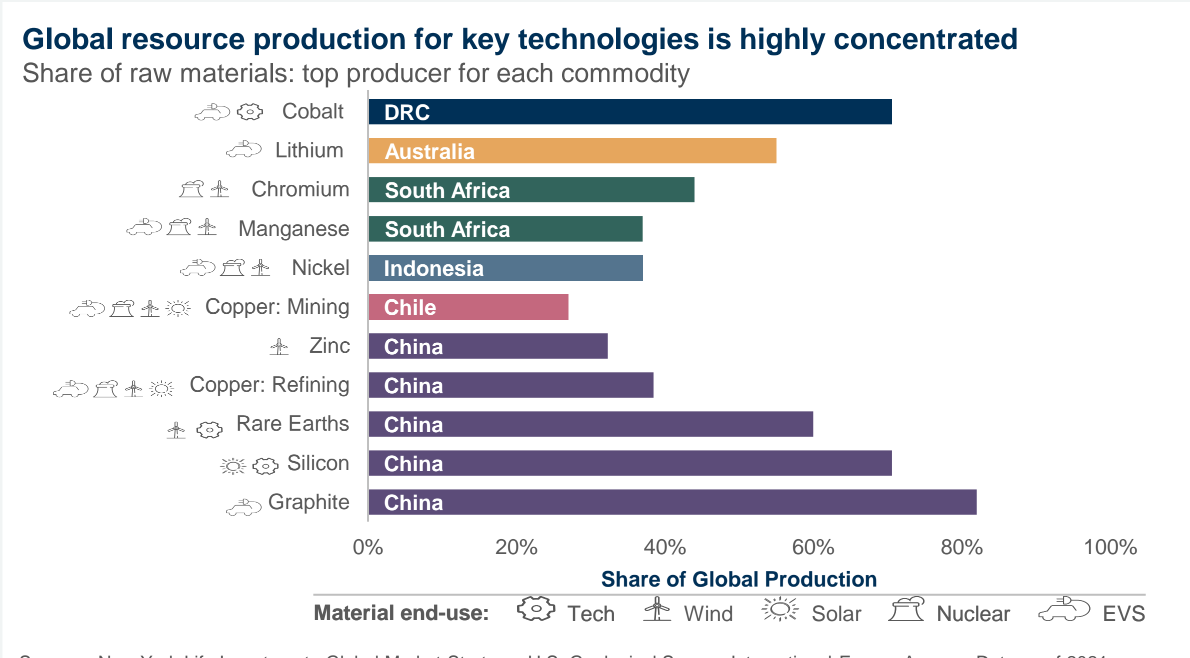
… and structural trends create persistent demand for capital

Global megatrends related to digitization, electrification, supply chains, and geopolitical risk create consistent demand

- A powerful combination of global economic and geopolitical events – the COVID-19 pandemic, the resulting inflation wave, the increasing visibility of climate change, Russia's invasion of Ukraine, the rapid rise in computing power of semiconductors — has rapidly changed the global economic model. Efficiency of supply chains is no longer as important as the security of, and persistent access to, key materials.
- We believe that the combination of national interest (public funding), corporate leadership (capital expenditure), and universal application (household interest) in these trends will result in durable investment.
- For the next few years, these transitions are likely to be highly capital intensive. More materials will be required, promoting potentially higher prices for those materials, and contributing to our conviction that inflation and interest rates are likely to be higher and more volatile.
- These transitions may also drive policy changes. Stickier inflation, alongside a strategic demand for capital investment, may encourage central banks to re-consider their inflation targets.



Sources: New York Life Investments Global Market Strategy, Macrobond, International Energy Agency, CBRE Investment Management, European Commission, China's State Council, Japan Science and Technology Agency, S&P Global, U.S. Energy Information Administration, June 2024. TWh = terawatt hours of electricity



Sources: New York Life Investments Global Market Strategy, U.S. Geological Survey, International Energy Agency. Data as of 2021.

2 High conviction investment ideas: U.S.

Assessing market opportunity

- Our top asset allocation picks

Key questions for the market

- Trump trades: fade or follow?
- Why are market rates rising when the Fed is easing?
- How do I invest for a normalizing yield curve?
- Are we heading for a double peak in inflation?
- Where can the AI trade go from here?
- How can I account for geopolitical risk?

How to invest our macro views

The bull-bear battles of 2025

	Fed Funds rate falling, but slower than before	Market rates likely to be higher and volatile	New policy creates new winners & losers	Persistent capital markets themes
Our view	Deploy cash to counter reinvestment risk	Tactical buying opportunities Cautious on duration	Fade partisanship Follow the fundamentals	Investors can participate in a durable set of a-cyclical investment anchors
How to invest it	Deploy cash into: Short duration credit (i.e. quality high yield, municipal bonds) High-quality leveraged loans This major market turning point creates an attractive, if narrow, window for allocating into private equity, credit, and real estate, in our view.	Yield curve volatility is likely to create tactical bond buying opportunities throughout the coming 6 months Yields may not have peaked: Upward-sloping municipal bond curves remain our preferred spot to add duration	Quality is king Large cap value offers a compelling earnings-valuation dynamic Magnificent 7 offer greater earnings quality than large cap growth as a whole Small cap upside is tactical We still like bipartisan sectors: defense, energy, infrastructure	Long-term investment waves: Energy independence Supply chain reshoring Digital infrastructure Broadening of the AI thesis Private markets expansion Accounting for geopolitical risk

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Key questions: fade or follow the Trump trades?

We "fade" highly partisan market moves and "follow" performance where policy change under the new administration may bolster existing trends

Impact of Trump's election victory on asset class performance

Asset class	Change from 10/7 to 1/2/2025 Since Trump odds passed Harris
Bitcoin	39.24
S&P 500 Growth	6.19
U.S. dollar (DXY)	4.43
Large cap	2.96
S&P 600 Small cap	0.87
Oil	-0.41
S&P 500 Value	-1.67
China equities	-3.81
EM equities	-4.72
Gold	-4.87
Europe equities	-5.36

Percentage change, % (axis: -10, -5, 0, 5, 10, 15, 20, 25, 30, 35, 40)

Sources: New York Life Investments Global Market Strategy, LBMA (London Bullion Market Association), Macrobond Financial AB, MSCI, S&P Global, Intercontinental Exchange (ICE), Macrobond, January 2025. The S&P 500 Index is an unmanaged index that is widely regarded as the standard for measuring large-cap U.S. stock market performance. Europe equities and China equities represent the associated MSCI indices. Past performance is not a guarantee of future results. It is not possible to invest in an index.

Trades to Fade

Small caps capture risk on sentiment
- No cyclical tailwinds, upside is only tactical here. Elevated market rates remain and expected to hold or rise. Strong outperformance isn't likely.

Gold lost its luster
- Gold's recent decline is probably due to fading election uncertainty. As policy and deficit concerns persist, doubts about this inflation hedge will likely diminish. Overweight gold.

Technology moves higher on lessened threat of antitrust
- Deregulation benefits can be dampened by tariff pressures along the supply chain. Limited upside drivers on existing earnings strength. Stay market weight.

Trades to Follow

U.S. 10-year yield moves higher
- As fiscal risk dynamics unfold, inflation and interest rates will likely move higher with volatility along the way. Overweight short duration; do not favor extending duration.

Dollar breaks out of 2 year trading range
- Tariffs and higher yields are strengthening the U.S. dollar. Amid U.S. outperformance and an abundance of liquidity, the dollar maintains its strength. Long USD exposure.

U.S. outperformance
- U.S. growth will likely continue to outperform relative to global peers. Stay selective within international exposure and consider use of currency hedges. Overweight U.S.

Trades to Monitor

Bitcoin
- Extremely strong performance after the election, but remain mindful of the historical volatility and risk-on nature of the asset class. Small allocation can serve as diversifier.

Financials
- Slight overweight to financials. Deregulation may not be a tailwind for regional banks which previously had ineffective oversight. A normalizing yield curve helps more.

TAKEAWAY: Follow trades supported by not just policy change over the next few quarters, but those bolstered by underlying economic and sector themes. Fade highly partisan trades and those that are entirely dependent on cyclical risk-on sentiment, including small caps and bitcoin.

Key questions: why are market rates rising when the Fed is easing?

Both the "Trump trade" and structural factors are pressuring long rates higher

10-Year Yield

Path of policy rate

Hawkish shift: Fed cannot cut as quickly or to the extent initially expected.

- Stronger than expected economy
- Stubborn above-target inflation
- Re-set of overly dovish easing expectations

… have all contributed to a backup in policy rate expectations, market-based Treasury and corporate yields, and even mortgage rates.

TAKEAWAY: The Fed is still easing, but not as much as many investors hoped.

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Inflation expectations

Rising inflation expectations are a catch-all for a range of policy possibilities under a second Trump administration:

- Tariffs: goods inflation
- Tax cuts and deregulation: greater economic growth stemming from corporate and household activity
- Immigration: border crackdown and possible deportations at scale may create a negative supply shock to the labor force, pressuring wage growth higher

TAKEAWAY: We cannot attribute specific causes to rising inflation expectations; what matters is that they are rising.

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Term premium (supply and demand)

"Red Wave" outcome has exacerbated existing factors biasing long yields higher:

- Debt sustainability concerns increasing likelihood of higher Treasury issuance/supply
- Political and geopolitical risk
- Investor preferences, including moderate sovereign rates in other major nations

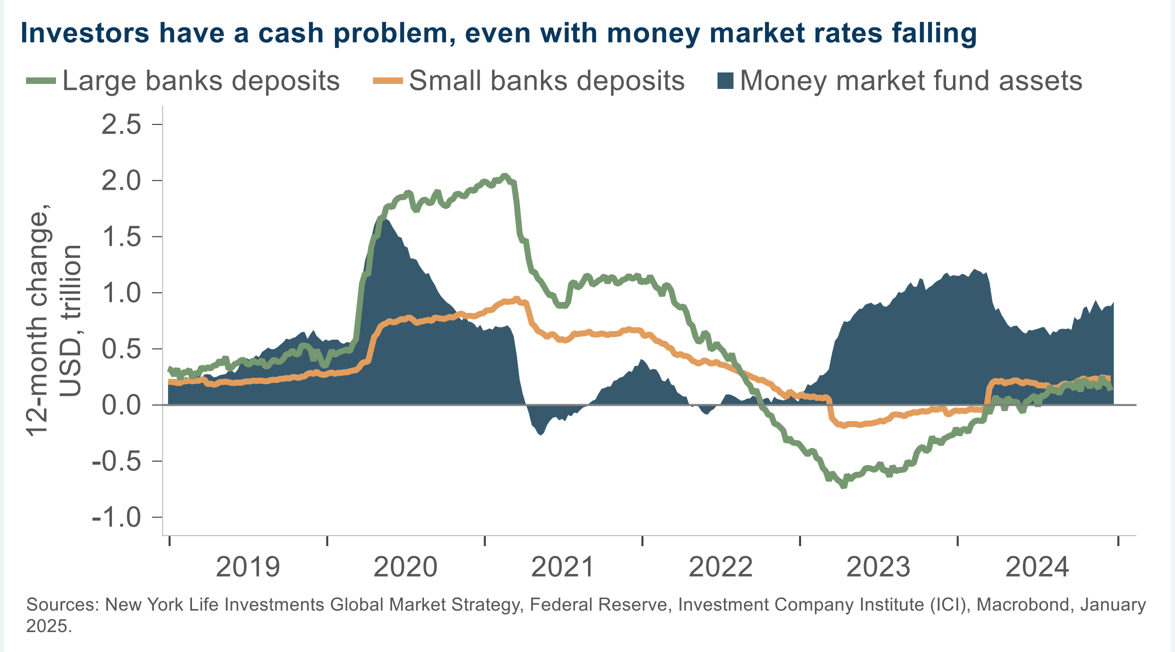
TAKEAWAY: Structural investment tailwinds are an upward pressure on long-term rates.

Opinions of New York Life Investments Global Market Strategy, January 2025.

Key questions: how do I invest the yield curve normalization?

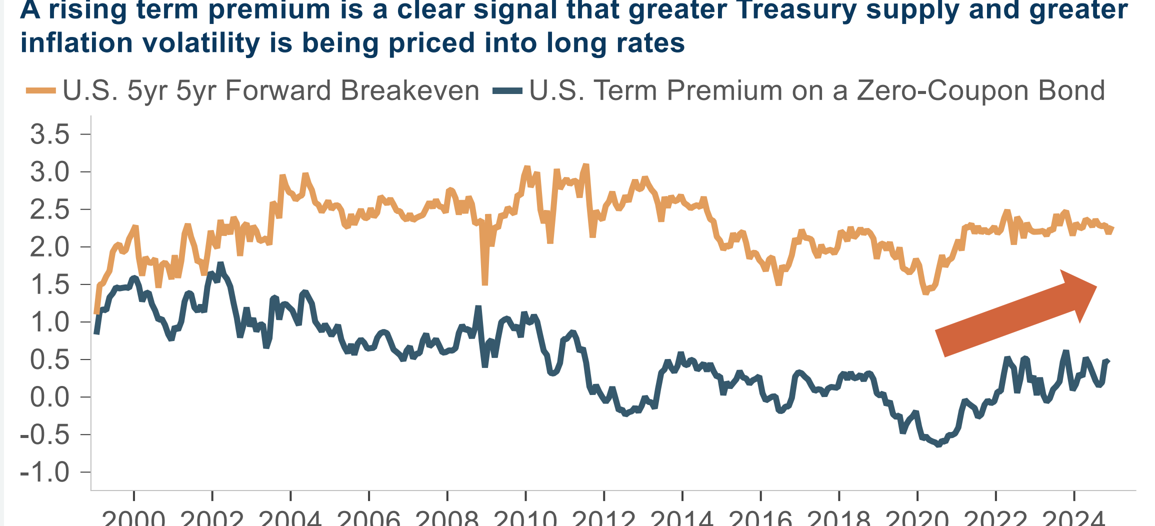
Cash deployment has an even more compelling value proposition as short rates fall and long rates rise

Investors have a cash problem, even with money market rates falling



Sources: New York Life Investments Global Market Strategy, Federal Reserve, Investment Company Institute (ICI), Macrobond, January 2025.

A rising term premium is a clear signal that greater Treasury supply and greater inflation volatility is being priced into long rates



Sources: New York Life Investments Global Market Strategy, Federal Reserve, University of Michigan, Macrobond, January 2025. The 5-year, 5-year forward breakeven measures inflation expectations beginning in 5 years for the following 5 years, often used as a measure of expected inflation volatility.

Deploying cash has an even more compelling value proposition as money market yields fall and yield volatility creates buying opportunities on the long end.

- Short rates: any investors are still over-allocated to cash, creating reinvestment risk as cash rates move lower. Though money market flows moved higher ahead of the U.S. election, they had begun to reflect rate cut expectations over the course of 2024 (**left chart**). We expect this repositioning to accelerate now that the timing of interest rate cuts has solidified.
- Long rates: since the pandemic, the term premium has moved up but remains moderate vs history (**right chart**). A rise in term premium around the 2024 election implies fears that greater Treasury issuance (supply) may be one sign of deteriorating debt sustainability. More volatile expectations for inflation exacerbate this fear.
- A normalizing yield curve has historically spurred private deal flow and credit creation. We believe that this may create an attractive, if narrow, window for allocating into private equity, credit, and real estate.
- Investors can consider pivoting from cash and into short-duration fixed income (high yield, investment grade) and adding duration in the upward-sloping municipal bond curves. Though credit spreads are likely to widen as economic growth slows, holding bonds to maturity can result in opportunities in both price appreciation and income generation.

Key questions: will we see a double peak in inflation?

There are strong parallels between today's economic backdrop and the factors driving double-peaks in inflation in the 1940s and 1970s

Historical examples of double peaks in inflation have a few similarities: artificially low interest rates, a major supply-demand shock, high budget deficits, and labor shortages. Major shifts in the global economic backdrop underpin these realities.

In the 1940s…

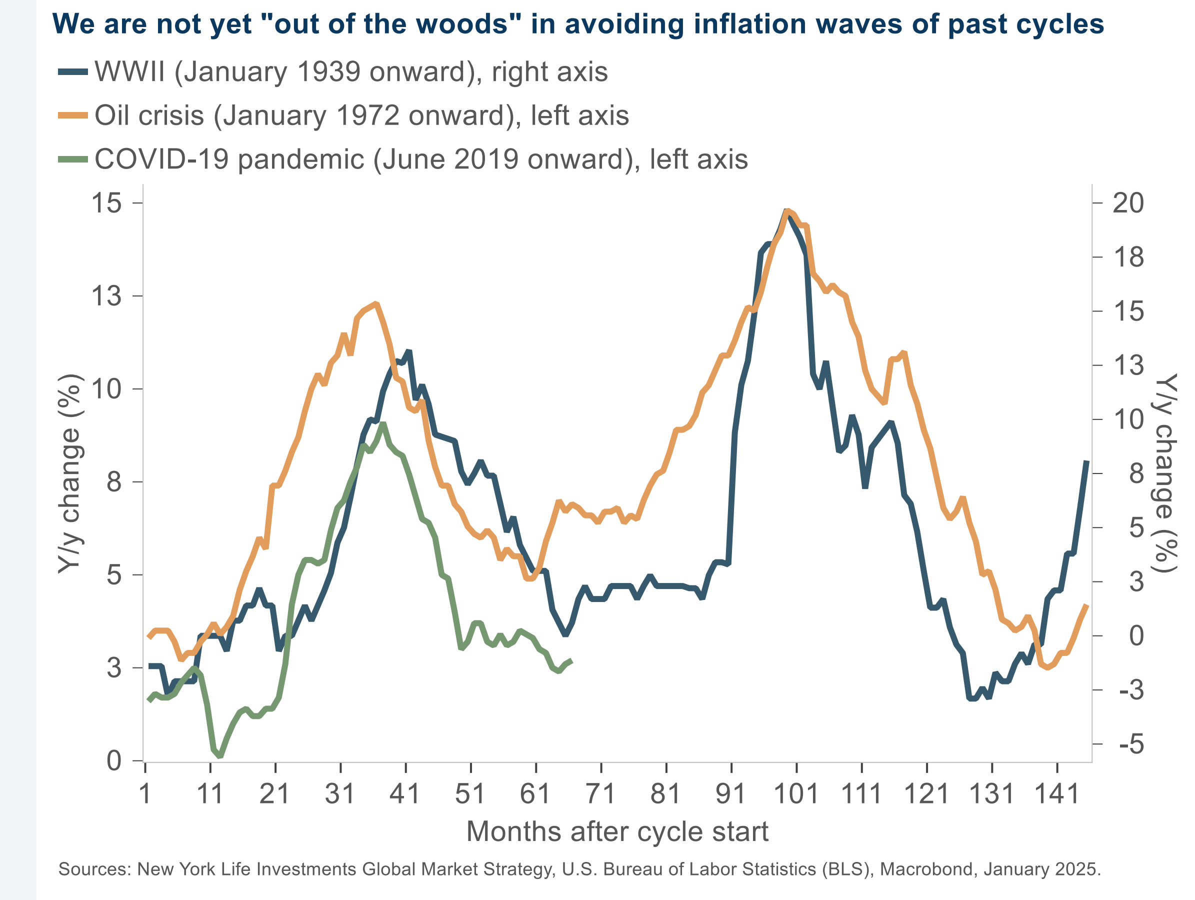
- World War II drove a massive labor shortage, goods shortage (including rationing), and extraordinary monetary policy (surge in money supply and artificially low rates to facilitate war financing) created the first wave in inflation.
- The double-peak in inflation was caused primarily by a second supply-demand shock. Pent-up demand from wartime rations was intensified as soldiers, themselves with pent-up savings, returned home. Labor shortages lingered in the near term, pushing wages higher.

In the 1970s…

- A supply-demand shock in energy (1973 oil embargo) pushed goods prices higher. Strong unions and wage-price spiral related to higher energy costs contributed to inflation. The Federal Reserve faced – and yielded to – significant political pressure to keep rates low.
- A second supply-demand shock in oil (the 1978 Iranian revolution), high budget deficit and labor shortage related to the Vietnam War, and a shortage of U.S. dollars related to the collapse of the Bretton Woods system contributed to the double-peak in inflation.

Today

- Supply-demand shocks in labor and goods related to the COVID-19 pandemic fueled inflation. Pandemic-era programs supporting consumer and businesses balance sheets extended it.
- A high budget deficit, supply chain re-globalization, and supply-demand shortages related to semiconductors (and energy to fuel them) could contribute to a double-peak in inflation. Revived labor shortages would likely be a trigger.

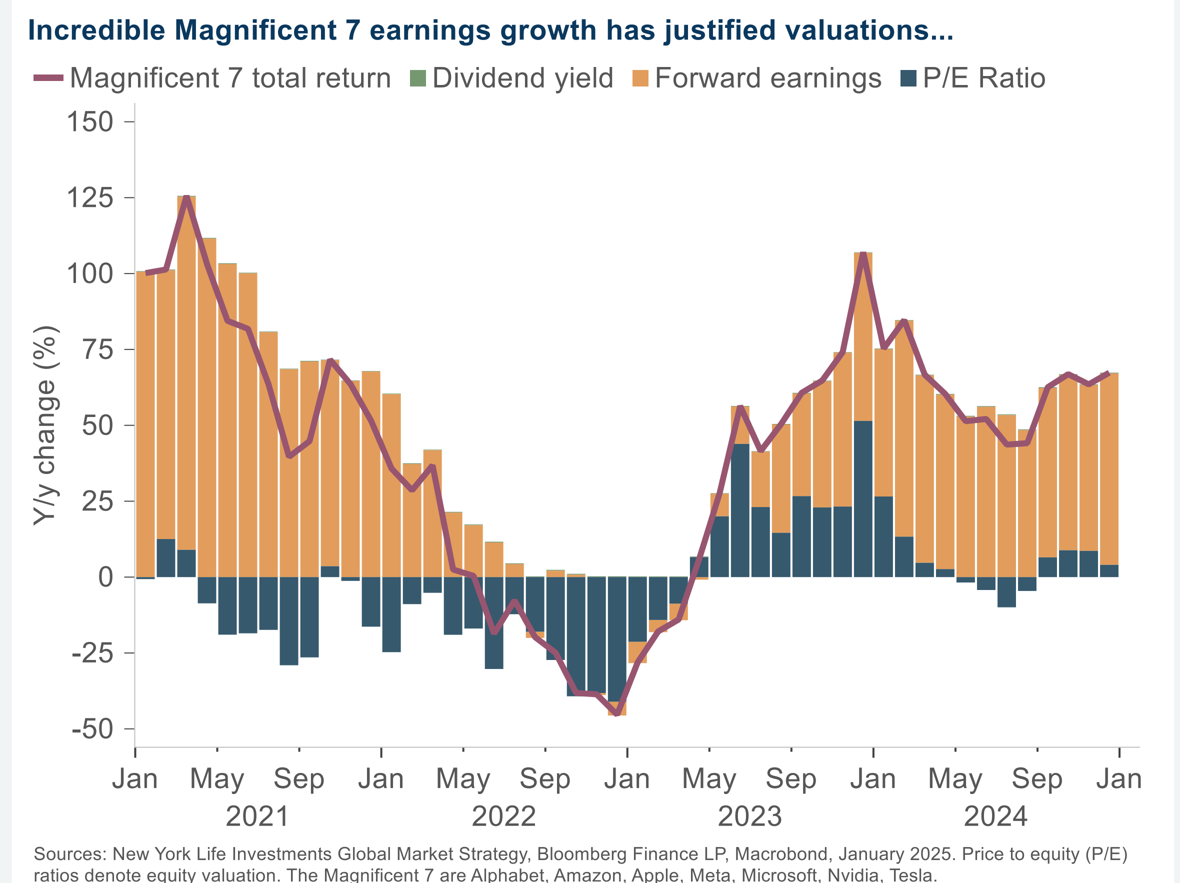


Sources: New York Life Investments Global Market Strategy, U.S. Bureau of Labor Statistics (BLS), Macrobond, January 2025.

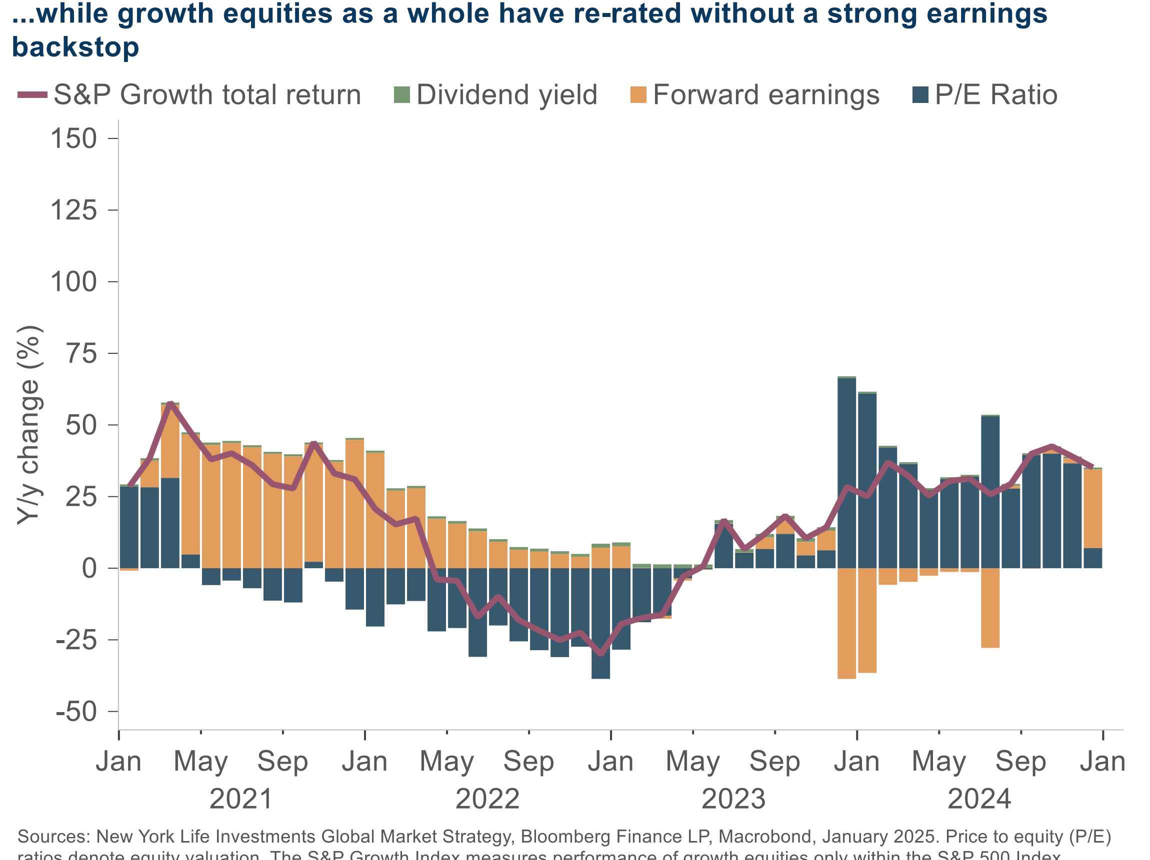
TAKEAWAY: There are many similarities between past experiences with double peaks in inflation and today. One important differentiating factor: political pressure to keep interest rates low has not yet materialized. We expect that inflation could re-firm from here; for inflation to move materially higher, we believe a change in central banks' mindsets toward inflation would be required.

Key questions: where can the AI trade go from here?

Ironically, the most “hyped” portion of growth equities, the Magnificent 7, provide greater earnings quality than growth equities as a whole



Sources: New York Life Investments Global Market Strategy, Bloomberg Finance LP, Macrobond, January 2025. Price to equity (P/E) ratios denote equity valuation. The Magnificent 7 are Alphabet, Amazon, Apple, Meta, Microsoft, Nvidia, Tesla.



Sources: New York Life Investments Global Market Strategy, Bloomberg Finance LP, Macrobond, January 2025. Price to equity (P/E) ratios denote equity valuation. The S&P Growth Index measures performance of growth equities only within the S&P 500 Index.

TAKEAWAY: While the Magnificent 7 have arguably overreached in terms of market dominance, they include robust earnings histories and outlooks that justify their valuations. Growth equities as a whole have piggybacked on the Magnificent 7’s valuation tailwind, but without a corresponding explosion of earnings potential, this re-rating appears to be more tenuous.

Key questions: how can I account for geopolitical risk? (1/2)

Geopolitical risk may increasingly be a fixture of macroeconomic developments and investor allocation

Geopolitical risk is higher today than it was in the 2010s

The Geopolitical Risk Index is an index that measures the occurrence of geopolitical events, threats, and conflicts

1990s average
2020s average
2000s average
2010s average
Geopolitical risk index

Index: 0, 50, 100, 150, 200, 250, 300, 350, 400, 450, 500, 550

1985, 1990, 1995, 2000, 2005, 2010, 2015, 2020, 2025

Gulf war
9/11 Attack
Invasion of Iraq
Invasion of Ukraine
London bombings
Hamas vs Israel

Sources: New York Life Investments Global Market Strategy, Matteo Iacoviello, Macrobond, January 2025.

How does geopolitical risk manifest?

Risk type	Event risk	Paradigm shift
Description	A one-off incidence; difficult to see (e.g. terrorist attack) or to time (e.g. escalation of known risks in Taiwan, the Middle East); can be calendared (e.g. election)	Sustained impact, often seen as a spread of impact from initial event risk into broader economic factors; impact can be difficult to attribute
Type of Impact	One-off repricing • Volatility • Currency • Macro factors: oil, gold, currencies	Steady-state repricing; durable shift in supply & demand • Inflation • Government bonds • Expected volatility
Size of impact	How expected was the event?	Did the disruptor last? Is it supported or underpinned by other global themes?

Opinions of New York Lie Investments Global Market Strategy, January 2025.

TAKEAWAY: The impact of event risks have tended to fade over time. Investors seeking resilience from these shifts can consider an allocation to macro volatility, discussed on the next page. Paradigm shifts are those event risks that are extended or exacerbated by some broader global economic context. For these, investors should consider the long-term impacts and allocate towards those themes.

Key questions: how can I account for geopolitical risk? (2/2)

Rising incidence of geopolitical risk may make changes in investor allocation appropriate on a tactical and structural basis

Owning macro volality may be the trade of the 2020s

The macro volatility portfolio is composed of an equal weight of gold, oil, and bitcoin

Sources: New York Life Investments Global Market Strategy, Macrobond Financial AB, Macrobond, January 2025.

What is a "macro volatility" allocation? Investors can use equal weights of gold, oil, and bitcoin to provide potential resilience against the asset classes most often impacted by un-anticipatable event risks. We apply this allocation as a small satellite exposure sourced from equity.

Potential strategies to address geopolitical risk

Theme		Approach		Investment Idea
Incidence of geopolitical risk appears to be rising	→	Add a macro volatility portfolio	→	Equal parts oil, gold, and bitcoin, implemented as a small satellite exposure sourced from equity
Event risk can impact any country or region	→	Most investors are underweight international exposure	→	Maintain or even increase international exposure
	→	Geopolitical risk manifests via currency volatility	→	50% currency hedged strategy
Exogenous events reinforce pre-existing trends	→	Consider long-term impacts to macroeconomic variables in addition to asset classes	→	Inflation-aware asset classes: infrastructure equity and bonds
Risk management is complex and multi-faceted	→	Careful credit analysis in all asset classes; eye on long-term trends	→	Active management

Opinions of New York Lie Investments Global Market Strategy, January 2025.

3 International economic & market outlook

Where are we in the global economic cycle?

- De-synchronized global growth
- Euro area
- Japan
- China
- Emerging markets ex-China
- U.S. Dollar

Where are we in the global economic cycle?

- During the pandemic and recovery in 2020 and 2021, driving economic forces were primarily global in nature. Most major regions faced synchronized economic contraction in 2020, met with meaningful fiscal and monetary policy stimulus.
- Now, the size and extent of that stimulus is generating a less synchronized recovery period (**chart**). Many countries, such as the United States and the euro area, are experiencing similar themes of inflation, tighter central bank policy, and slowing growth – but with differing intensity. Others, such as Japan and China, are adapting to structural changes, which distinguishes their business cycles and investor opportunity sets.
- Globally, the re-shaping and redundancy of supply chains is refocusing in vestment in technology, energy, and financial infrastructure.

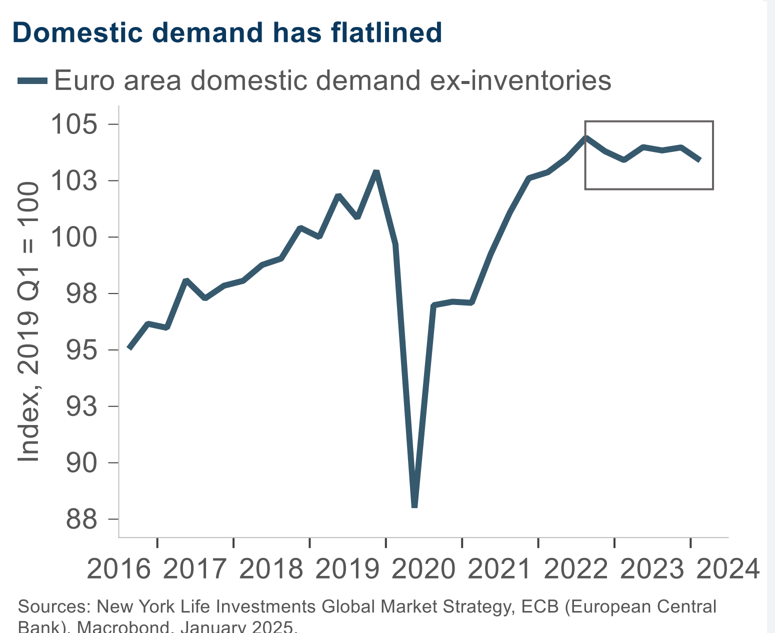
Major countries and regions face disharmonious economic growth dynamics and policy approaches

Sources: New York Life Investments Global Market Strategy, January 2025. For illustrative purposes only. "EM" is short for emerging markets. *The trough of an economic cycle is the lowest point in economic growth for a country during an economic cycle- A trough does not necessarily mean that there is a recession, but rather depends on the economic cycle.

Euro area

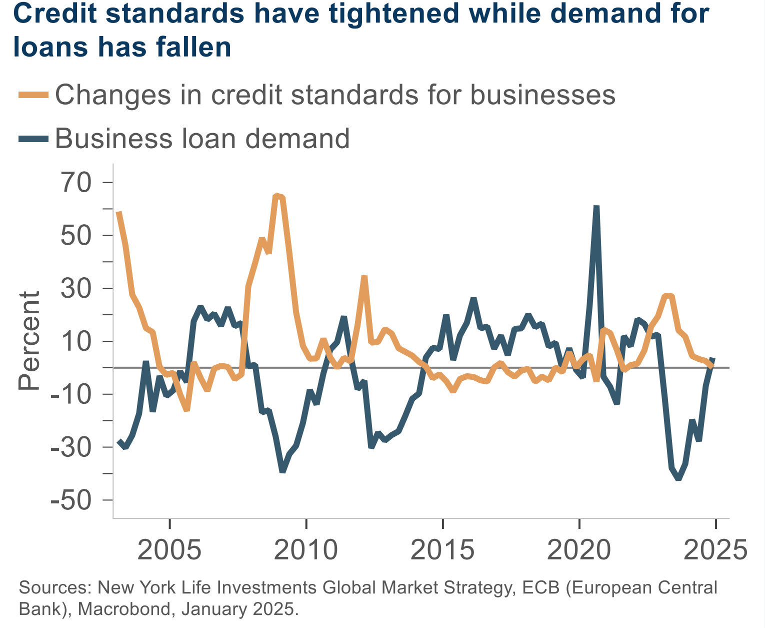
The euro area business cycle has been less pronounced than the U.S., but faces similar tradeoffs between high wages and tight credit conditions

- Since the COVID-19 pandemic, Europe has faced many of the same challenges as the U.S. Supply chain dynamics and labor force disruptions contributed to high inflation. Russia's invasion of Ukraine materially impacted gas prices, adding to inflation and growth concerns.
- Key differences with the U.S., such as a broad return to office work and fiscal support focused on social stabilizers (over stimulus checks) resulted in a more subdued business cycle.
- In the past year, euro area domestic demand has flatlined (**left chart**) and inflation has moved lower (**middle chart**). In response, the ECB began steadily cutting interest rates in June. As a result, credit conditions improved, and business loan demand moved higher (**right chart**).
- Still, we have tepid expectations for European activity. Challenges related to government investment, global trade, and low productivity drive this perspective.



Sources: New York Life Investments Global Market Strategy, ECB (European Central Bank), Macrobond, January 2025.

Sources: New York Life Investments Global Market Strategy, ECB (European Central Bank), Eurostat, Macrobond, January 2025.



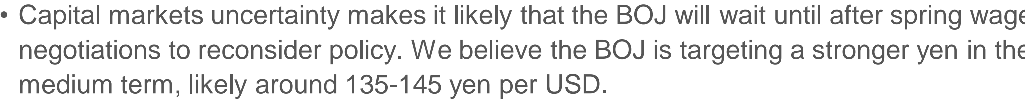
Sources: New York Life Investments Global Market Strategy, ECB (European Central Bank), Macrobond, January 2025.

TAKEAWAY: We expect tepid euro area growth because of timid consumption, low consumer confidence, and increasing challenges related to global trade and investment. That said, a consistent interest rate cutting cycle may create investment opportunity. A quicker valuation bottoming process combined with attractively priced currencies may create a tactical opportunity later in 2025.

Japan

Interest rates are on the rise for the first time in decades, creating near term challenges to otherwise positive structural policy change

- While most global central banks were raising rates in the last two years, the Bank of Japan maintained accommodative monetary policy. This has now reversed. A weaker yen spurred import-price inflation, contributing to higher wages for the first time in many years (**left chart**). In response, the Bank of Japan (BOJ) loosened yield curve control, then ended negative interest rate policy in March, and has now hiked rates to 0.25% in July. Market financial conditions, including equity market valuations, have tightened considerably in response.

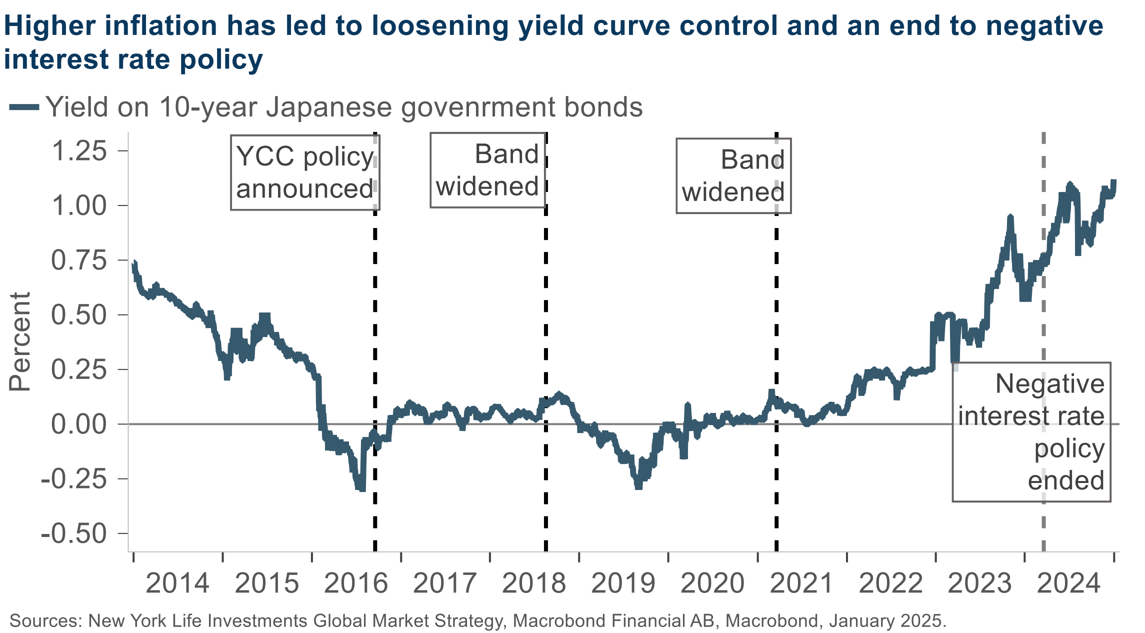


- Capital markets uncertainty makes it likely that the BOJ will wait until after spring wage negotiations to reconsider policy. We believe the BOJ is targeting a stronger yen in the medium term, likely around 135-145 yen per USD.
- At the same time, the government and private sector have made meaningful changes to promote competitiveness, improving global corporate and investor expectations for Japan's long-term growth and investment attractiveness.

Negotiations lead to steepest wage increases in 30 years

Sources: New York Life Investments Global Market Strategy, Japanese Trade Union Confederation (RENGO), Japanese Statistics Bureau, Ministry of Internal Affairs & Communications, Macrobond, January 2025.

Higher inflation has led to loosening yield curve control and an end to negative interest rate policy

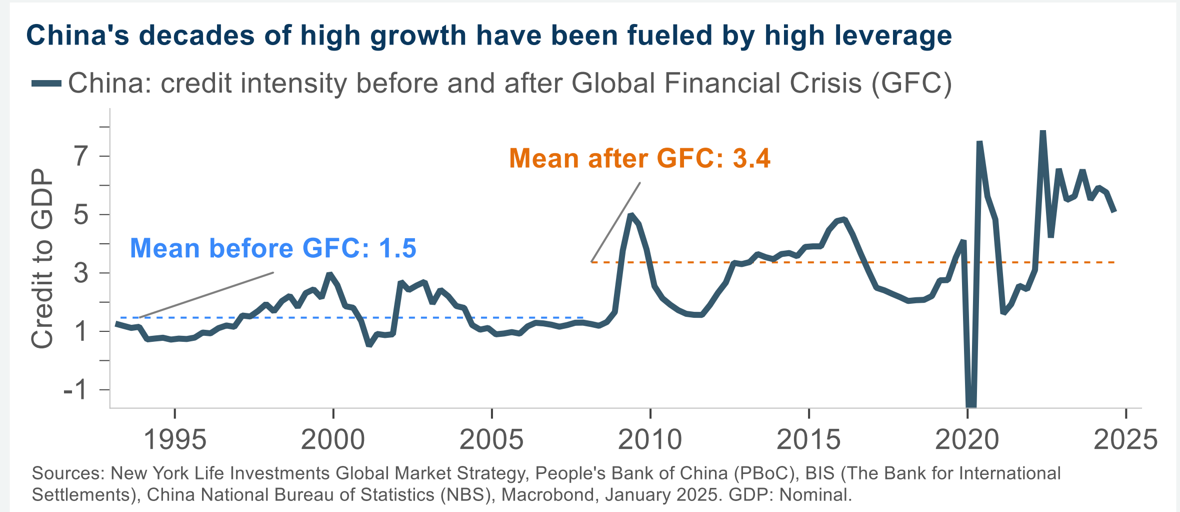


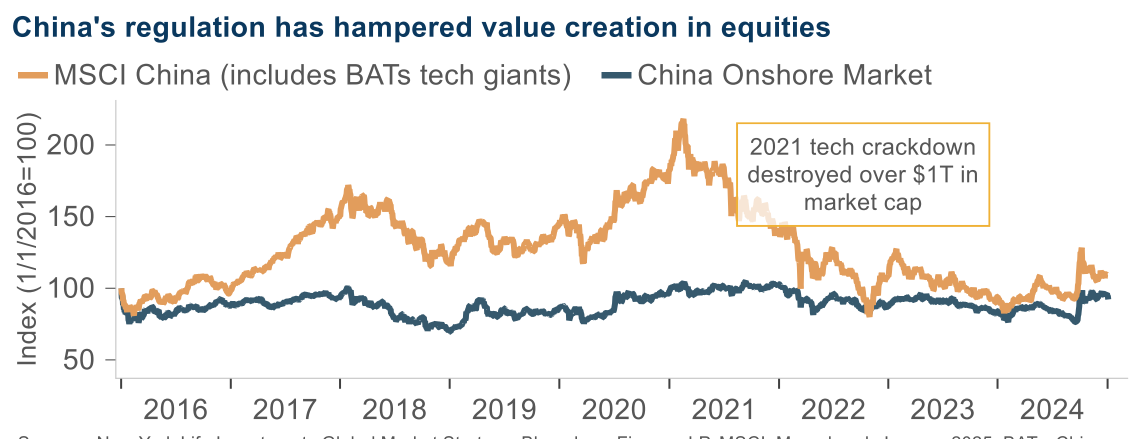
Sources: New York Life Investments Global Market Strategy, Macrobond Financial AB, Macrobond, January 2025.

TAKEAWAY: Despite Japan's technical recession, we believe the country's re-orientation towards global competitiveness may persist, potentially improving productivity and economic activity. We are closely watching recent developments in the semiconductor supply chain, which could position Japan as an incremental chip manufacturing location, and therefore increase capital investment.

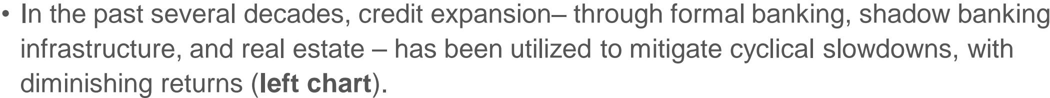
China's structural story

A deleveraging problem and illiberal capital markets policy are likely to constrain investment opportunities over the medium term





Sources: New York Life Investments Global Market Strategy, Bloomberg Finance LP, MSCI, Macrobond, January 2025. BATs: Chinese tech giants listed outside China's onshore markets: Baidu, Alibaba, Tencent. Onshore markets represented by Shanghai Composite, comprising all A and B shares listed in Shanghai. MSCI China: large and mid-cap represenation across Shanghai and Shenzhen.



- In the past several decades, credit expansion– through formal banking, shadow banking, infrastructure, and real estate – has been utilized to mitigate cyclical slowdowns, with diminishing returns (**left chart**).
- Recent years' policies seem to acknowledge that the high-leverage model is unsustainable: shadow lending had slowed, Chinese real estate giant Evergrande was allowed to fail, and local and central government growth targets have been periodically relaxed.
- But in this cycle, the taps have been turned back on. In 2025 Chinese growth is expected to slow from 5.2% YoY to 4.8% - with pressure from a property crisis and a weakening jobs market alleviated by central government financing.

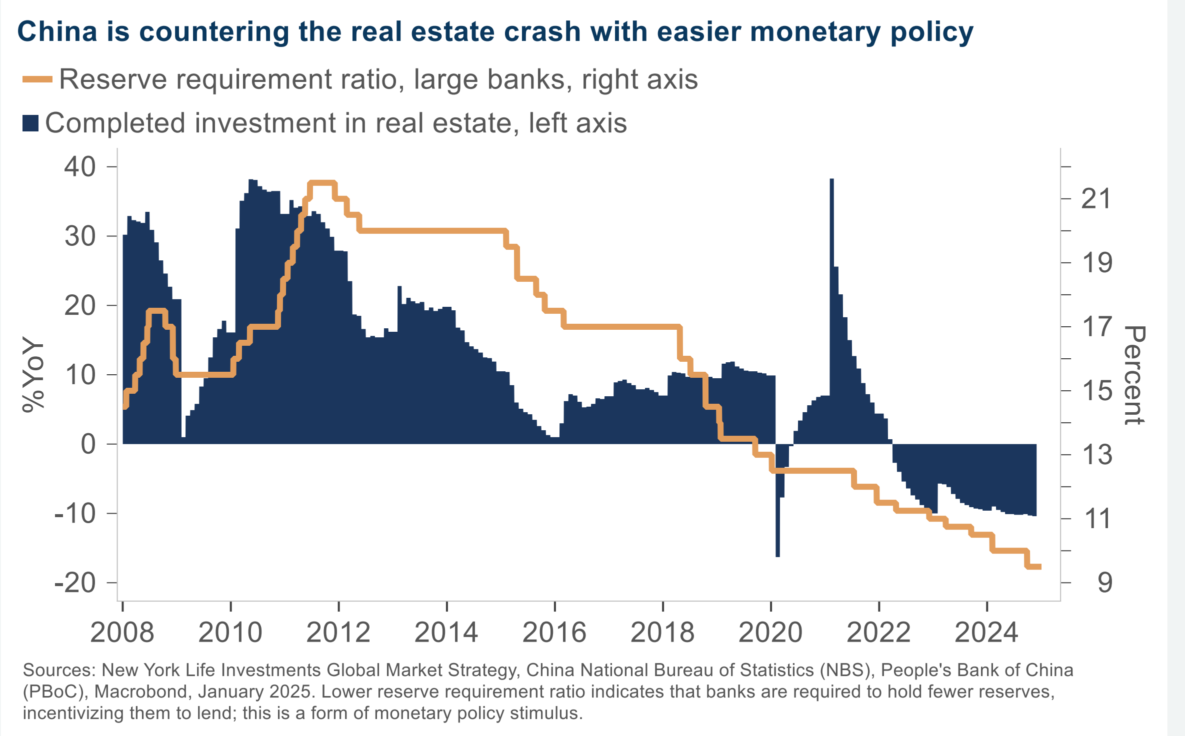
- China's closely regulated onshore equity markets do not include exposure to major tech firms, including the BATs: Baidu, Alibaba, and Tencent, which operate within China but are listed primarily in the U.S. (**right chart**). Lack of onshore exposure to these names enabled China's infamous tech crackdown of 2021, where harsh new regulations and fines against these firms destroyed over $1T in market cap for U.S.-listed China indexes.
- While China made decades of great strides to liberalize its capital markets, recent years have seen a slew of anti-investor regulation that has harmed market confidence in the country.
- Other structural issues on our radar: demographics, productivity, intellectual property protection.

TAKEAWAY: China remains the world's #2 economy and trade power, and in this sense continues to be a "must have" in a diversified international allocation. However, the country's proclivity for avoiding economic growth slowdowns with the use of leverage, paired with wavering investor-friendly policies, make us cautious on the medium-term outlook.

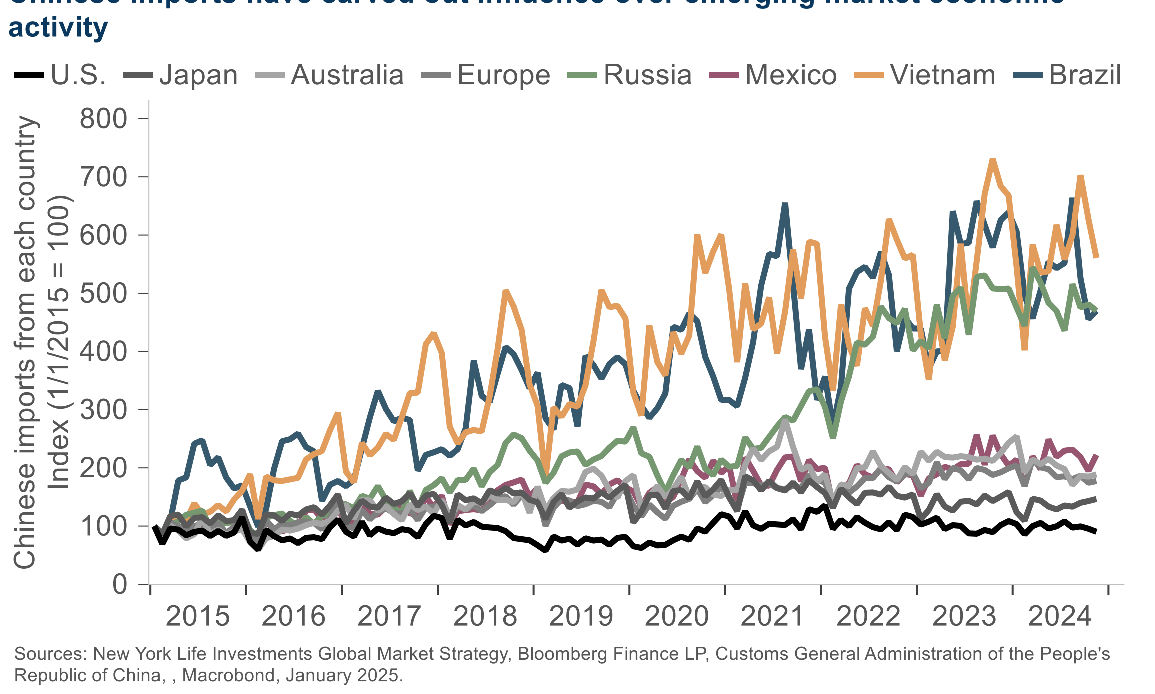
China's cyclical story: managing the extent of the slowdown

China's stimulus is not meant to spark an economic acceleration, possibly to the detriment of key Emerging Market trade partners

- China's 2024 stimulus is nothing new relative to its history and is not a bazooka capable of re-accelerating the economy. This cycle and on a structural basis, China uses monetary policy to counterbalance the real estate market, in part by reducing required reserve holdings by banks to encourage lending when real estate is in contraction (**left chart**). Given the extent of real estate recession in China, we believe this stimulus is meant to control the extent of total economic slowdown rather than foster an outright economic acceleration.
- China's import power over many emerging markets (EMs, **right chart**) means that if China is slowing, EMs will feel the pressure via slower demand for their exports. We expect China's deceleration – both cyclical and structural – to add to global growth pressures already emanating from the U.S. and Europe.
- There is anecdotal evidence suggesting that even when China is slowing, its commodity demand remains resilient, potentially putting a structural "floor" under industrial metals and gold prices.



Sources: New York Life Investments Global Market Strategy, China National Bureau of Statistics (NBS), People's Bank of China (PBoC), Macrobond, January 2025. Lower reserve requirement ratio indicates that banks are required to hold fewer reserves, incentivizing them to lend; this is a form of monetary policy stimulus.

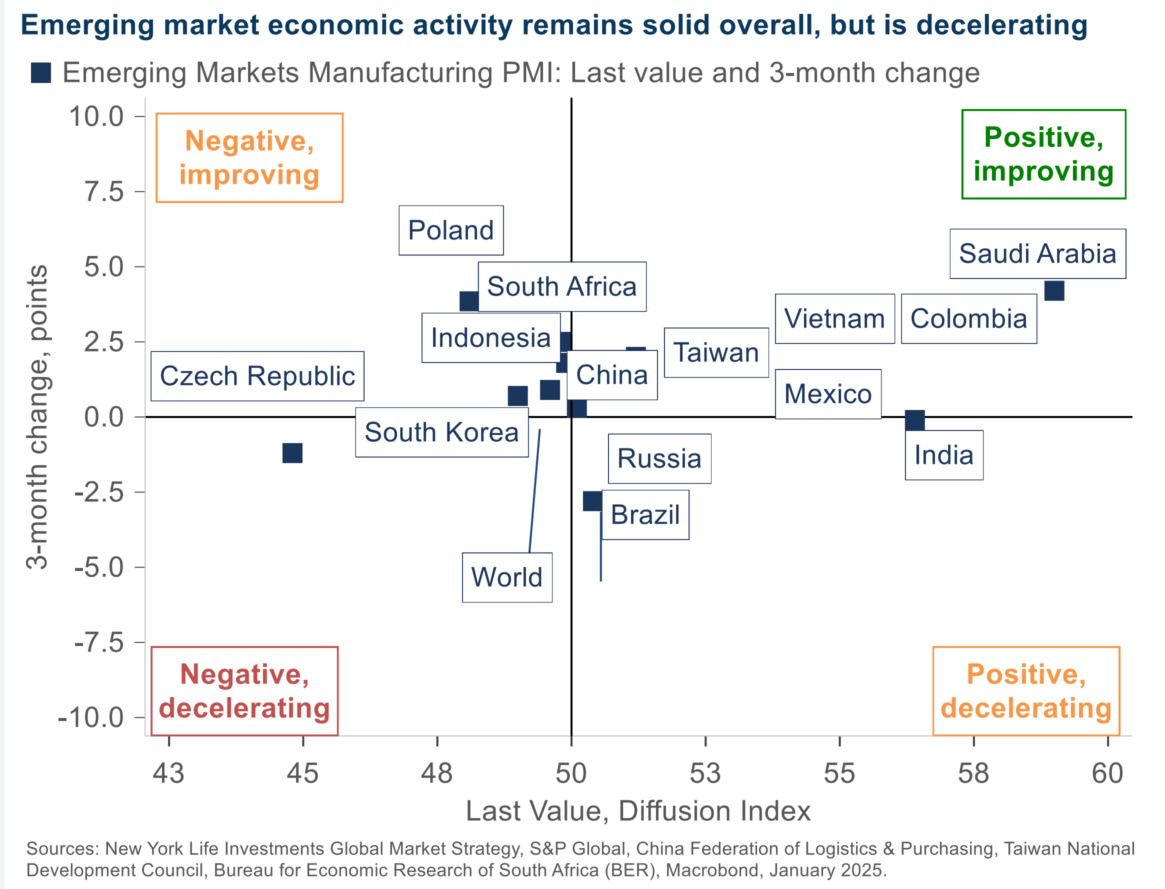


Sources: New York Life Investments Global Market Strategy, Bloomberg Finance LP, Customs General Administration of the People's Republic of China, , Macrobond, January 2025.

Emerging markets

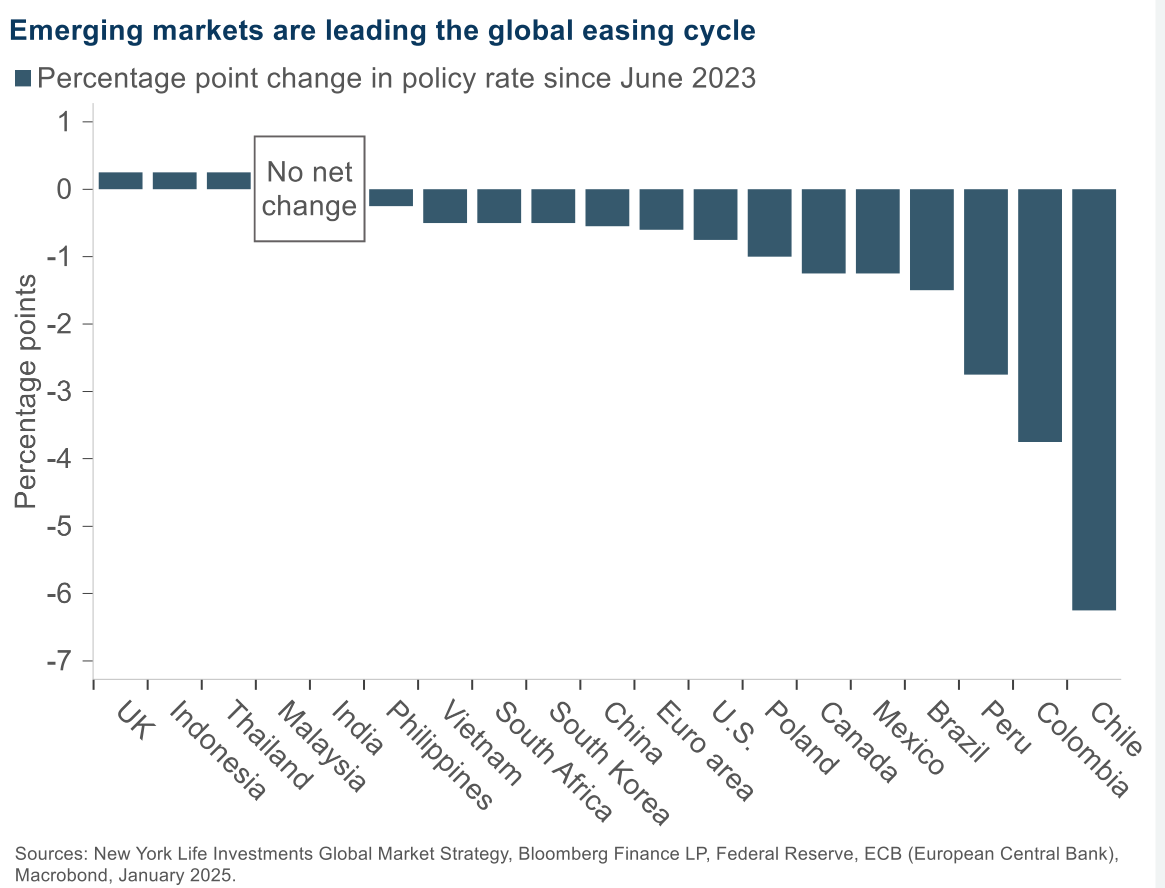
"When the U.S. sneezes, Emerging Markets catch a cold": cyclical pressures visible in EM

Emerging market economic activity remains solid overall, but is decelerating



Sources: New York Life Investments Global Market Strategy, S&P Global, China Federation of Logistics & Purchasing, Taiwan National Development Council, Bureau for Economic Research of South Africa (BER), Macrobond, January 2025.

Emerging markets are leading the global easing cycle



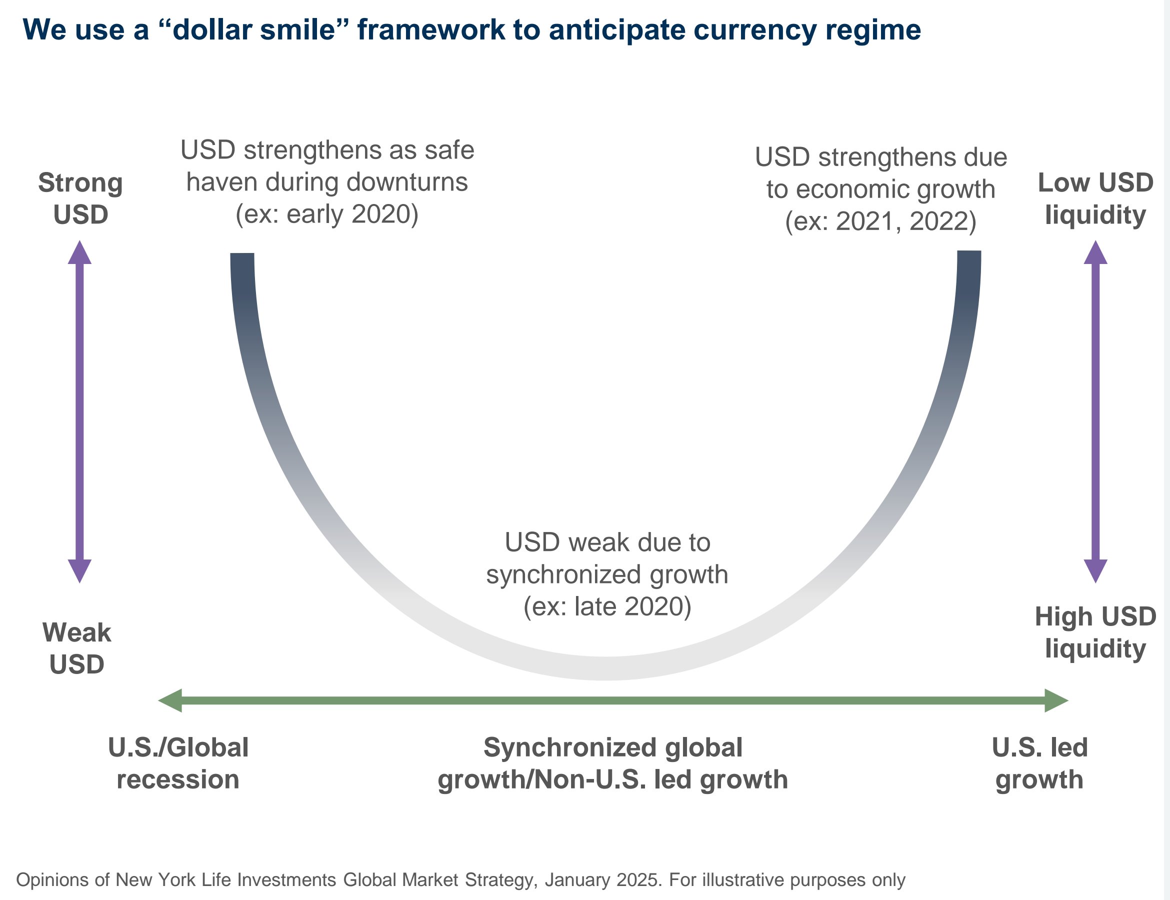
Sources: New York Life Investments Global Market Strategy, Bloomberg Finance LP, Federal Reserve, ECB (European Central Bank), Macrobond, January 2025.

TAKEAWAY: Emerging markets are heterogenous, but historically struggle to overcome growth pressures from developed markets. Investors should be sensitive to the earnings and valuation outlooks in each market, or should consider a holistic hedging strategy to counter broad-based EM currency weakness in periods of slowing global growth (for more, see asset class insights).

U.S. dollar likely to strengthen as global economies slow

The strength of the U.S. dollar has been bolstered by strong U.S. economic growth; ahead, dollar strength may come more from a flight to safety

We use a "dollar smile" framework to anticipate currency regime



Opinions of New York Life Investments Global Market Strategy, January 2025. For illustrative purposes only

The dollar smile

- We see the strength or weakness of the U.S. dollar as a key source of risk for international exposure. One useful framework for analyzing the dollar is the "dollar smile" (**chart**). In moments of low liquidity (such as a crisis or recession), or when U.S. economic growth outperforms, the dollar is likely to be stronger. When liquidity and global growth are ample, the dollar tends to weaken.

Moving from left to right on the dollar smile curve:

- The dollar strengthened at the start of 2020, when a flight to quality fueled dollar demand.
- Later, the global economy grew as countries recovered from the COVID-19 pandemic. The broad and synchronized expansion led to dollar weakness in the second half of 2020.
- In 2021 and 2022, the dollar strengthened as U.S. economic growth, supported by large fiscal and monetary stimulus, began to far outpace that of other countries.
- The dollar has since settled just above its historical average, and it sits on the right side of the smile. We expect dollar strength to persist if the U.S. economy joins the global slowdown, i.e. move to the left side of the smile.

What would bring U.S. dollar weakness?

- For the U.S. dollar to weaken (i.e. move towards the bottom of the "dollar smile"), we would likely need to see a robust reacceleration of global growth that overtakes that of the U.S.
- Rate cuts from the Fed may also reduce the USD's attractiveness relative to other currencies in the short term though rate differentials still favor the USD.
- Trump's proposed tariffs (10% flat tariff, 60% on imports from China) could reduce dollar demand, and therefore see the dollar weaken on a relative basis.

TAKEAWAY: Leading indicators point to slowing global economic growth and even recession in many major economies. This supports U.S. dollar stability or even strengthening from here. Investors with global exposure can consider a currency hedged strategy.

Dollar dominance: the U.S. dollar remains chief of all reserve currencies

The Chinese renminbi in particular does not yet meet the criteria for reserve currency status, and is unlikely to pose a threat to dollar dominance

REQUIREMENTS FOR A GLOBAL RESERVE CURRENCY

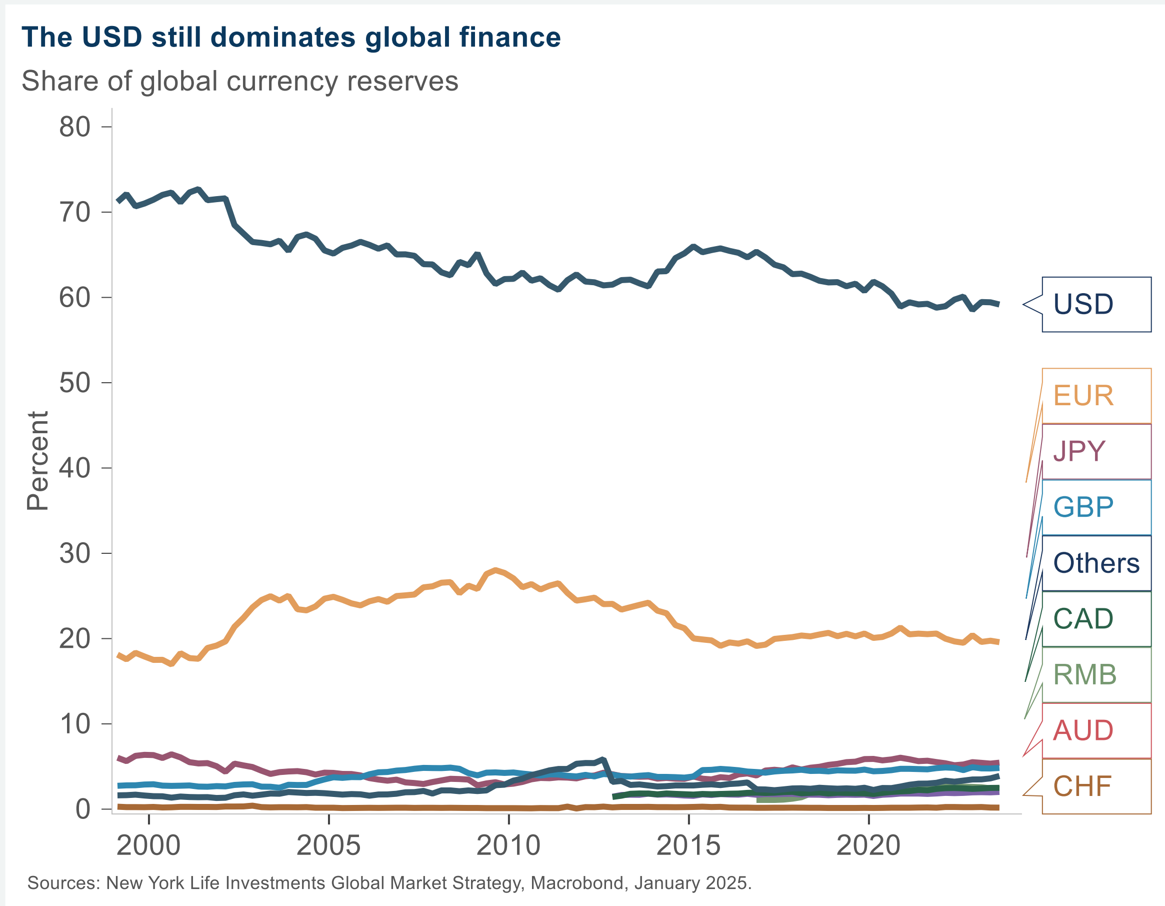
REQUIREMENT	U.S. DOLLAR	EUROPEAN EURO	JAPANESE YEN	CHINESE RENMINBI
Trust in the central bank *Foreign holding of government debt*	59%	20%	6%	2%
Liquidity *Foreign holding of government debt*	35%	38%	30%	9%
Broad acceptance *Share of foreign currency debt issuance*	64%	24%	3%	1%
Convertibility *FX transaction volume*	45%	16%	9%	4%
Open capital account *Capital controls*	**None** (Open)	**None** (Open)	**Some** (Restrictions)	**Tight** (Closed)
Floating exchange rate regime *Exchange rate regime*	**Floating**	**Floating**	**Managed** (Yield curve control)	**Managed** (against a basket of currencies... including the U.S. dollar!)

Sources: New York Life Investments Global Market Strategy, Federal Reserve, Bank for International Settlements, Bloomberg Finance LP. January 2025. FX refers to foreign exchange. The Chinese currency can be referred to interchangeably as the renminbi or the yuan.

TAKEAWAY: Dominating global reserves, transactions, and global debt, the USD is set to remain the world's primary reserve currency. China's capital controls and lack of global convertibility and transactability make it unlikely for RMB influence to expand beyond select commodity-based trade relationships.

Dollar dominance: only innovation can unseat the USD

Real disruptive potential comes not from competitor currencies, but innovation



- What could truly pose a threat to the vast scale of USD dominance (**left chart**)?
- History tells us that a combination of innovation and global conflict have been the catalysts for currency regime change (**table**). It is not a country's rise in importance, but rather the emergence of a new and more efficient system, that has initiated past currency transitions. Digital currencies could be the next such innovation to disrupt today's currency regime.

DOMINANT CURRENCY	MAINSTREAM VIEW FOR DOMINANCE	INNOVATION CATALYST
Venetian ducat (12th century–16th century)	The Fourth Crusade and other medieval military conflicts	Gold standard, minting and navigation technology
Spanish dollar (16th century–1800)	Spanish Armada's defeat of the English navy in 1588	Mining and transportation technology
British pound (1815–1920)	The Seven Years' War and the Napoleonic Wars	Steamship industry expansion
U.S. dollar (1920–?)	WWI, WWII	Early adoption of telegraph, federal reserve system, development of aviation industry

TAKEAWAY: Though countries like China are increasing in global geopolitical importance, it is not a single country's rise that displaces a currency – at least in historical terms. Instead, we expect the U.S. dollar system would be more likely to be replaced when a more efficient alternative to fiat currencies – such as a global digital currency system – were to emerge.

4 Global asset class insights

Risk

- Risk preference
- Equity risk premium

Equity

- Corporate earnings
- Style
- Size
- Non-U.S. developed markets
- Emerging markets

Credit

- Credit overview
- Investment-grade
- High yield
- Bank loans
- Convertible bonds
- Municipal bonds

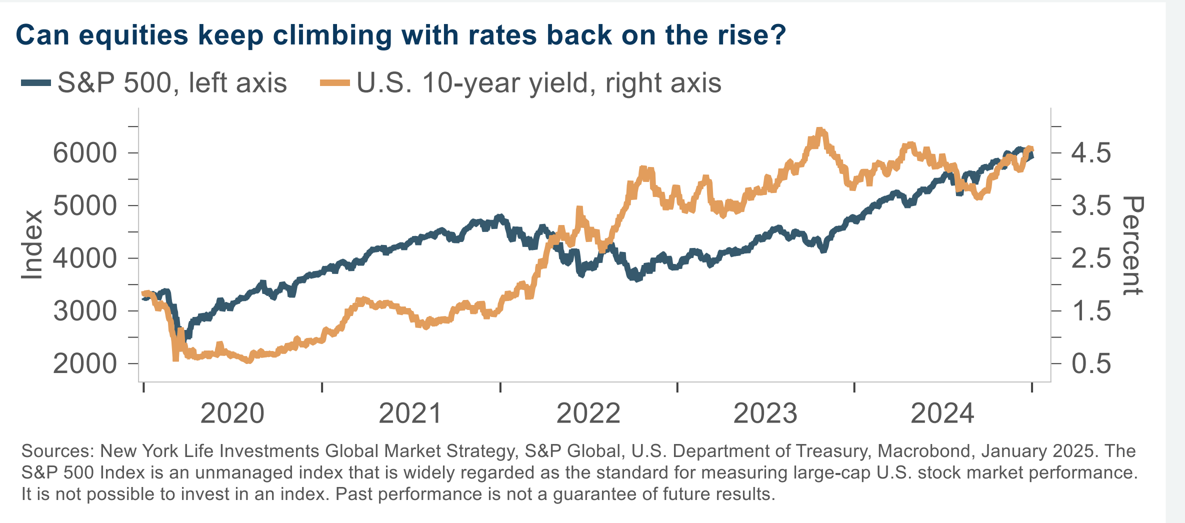
Alts

- Alternatives through the cycle
- Infrastructure
- Commodities
- Liquid real estate

Steady macro environment for stocks and bonds

A resilient corporate background means it may not be the time for wholesale profit taking, but we still favor taking incremental risk in credit

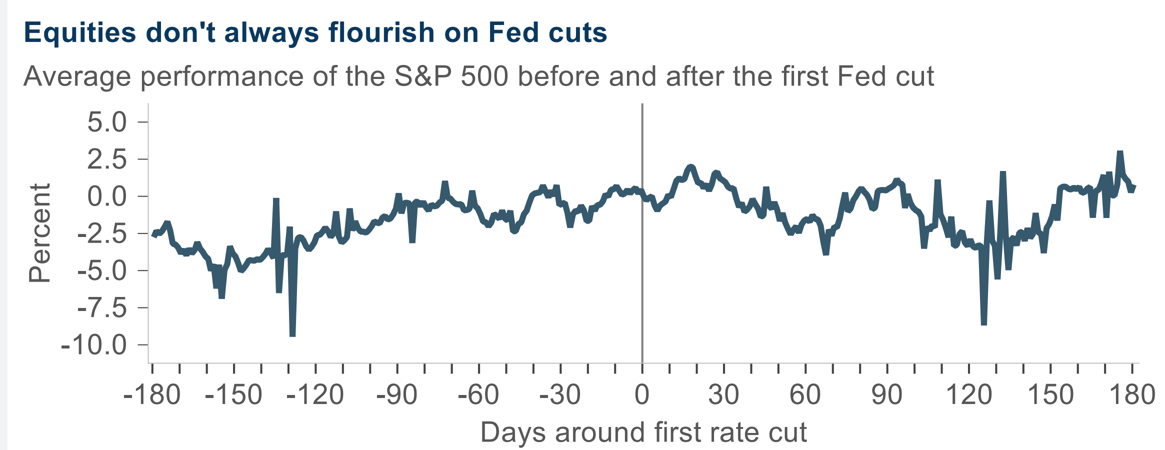
Can equities keep climbing with rates back on the rise?



Sources: New York Life Investments Global Market Strategy, S&P Global, U.S. Department of Treasury, Macrobond, January 2025. The S&P 500 Index is an unmanaged index that is widely regarded as the standard for measuring large-cap U.S. stock market performance. It is not possible to invest in an index. Past performance is not a guarantee of future results.

Equities don't always flourish on Fed cuts

Average performance of the S&P 500 before and after the first Fed cut



Sources: New York Life Investments Global Market Strategy, S&P Global, NBER (National Bureau of Economic Research), Macrobond, January 2025. Index performance is not a guarantee of future results. It is not possible to invest in an index.

- The U.S. equity market continues to reach new highs amid interest rate volatility (**left chart**). The S&P 500 has been on a historic run, defying forecasters' expectations and ignoring the warning signs of leading economic indicators. Market optimism, especially, had risen as the Fed has started cutting interest rates – but has not faded amid the backup in interest rates seen in October. Though we are cautiously optimistic on economic growth, we are not convinced of a reacceleration. We believe investors could be most compensated by taking incremental risk in credit.
- Investors have felt pressure as rates continue rising despite the start of Fed cuts and normalization of the U.S. 10-year/2-year yield curve. We see the short end of the curve repricing on stronger growth, persistent inflation, and the possibility of slower rate cuts. The long end is moving in response to potential deficit impacts from future fiscal policies, in our view.
- While many equity investors anticipated relief from easier monetary policy, the S&P 500 has risen only about 4% since the Fed's September rate cut. Rate cuts don't always drive equity gains (**right chart**), particularly when cuts coincide with slower growth. When the economy is not in recession, Fed cuts have limited effect on equities. If the economy is in recession, Fed cuts often fail to provide substantial support to equities.

TAKEAWAY: The soft landing environment of the past nine months has been supportive of stocks and bonds. While we see both upside and downside risks, we don't think investors should sit out altogether. We believe there are compelling investment opportunities, but at this point in the cycle investment selectivity is more important.

Understanding the equity risk premium as a long-term indicator

Will equities continue to outperform bonds? Today's equity risk premium suggests the answer may be yes

The U.S. equity risk premium is a weak indicator of one year excess performance of stocks over bonds...

Individual dots represent months, data from 1980

1-year real excess return (%)

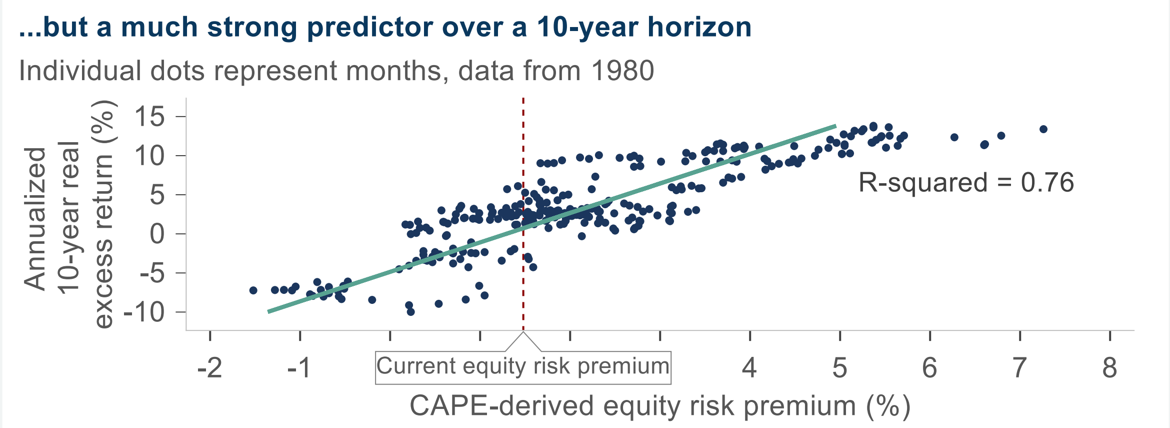
R-squared = 0.08

CAPE-derived equity risk premium (%)

Sources: New York Life Investments Global Market Strategy, Shiller, Macrobond, January 2025. R-squared quantifies how much of the variation in the dependent variable is explained by the independent variables in a regression model. CAPE: cyclically adjusted (for inflation) price-to-earnings ratio.

...but a much strong predictor over a 10-year horizon

Individual dots represent months, data from 1980



Sources: New York Life Investments Global Market Strategy, Shiller, Macrobond, January 2025. R-squared quantifies how much of the variation in the dependent variable is explained by the independent variables in a regression model. CAPE: cyclically adjusted (for inflation) price-to-earnings ratio.

- The equity risk premium measures the difference between the expected return from equities (the earnings yield or inverse of the price-to-earnings ratio) and the risk-free return (typically the U.S. 10-year Treasury yield). A low or negative equity risk premium implies that equities are potentially overvalued relative to bonds, suggesting a lower likelihood of equities outperforming bonds.
- As a predictor, the equity risk premium has historically done a weaker job on a short-term time horizon. There is virtually no relationship between the equity risk premium and one-year ahead returns suggesting equity risk premium is a weak predictor of year ahead returns (**left chart**).
- However, over a 10-year horizon, the equity risk premium has historically been a much better predictor of future returns (**right chart)**. Based on historical experience, today's equity risk premium would point to an annualized 10-year real outperformance of stocks over bonds of roughly 1.5%. This says to us that there is more risk to buying equities at these levels and outperformance of stocks over bonds is challenging in this environment..

TAKEAWAY: Based on current market valuations and interest rate levels, expecting stocks to significantly outperform bonds over the next decade might be overly optimistic.

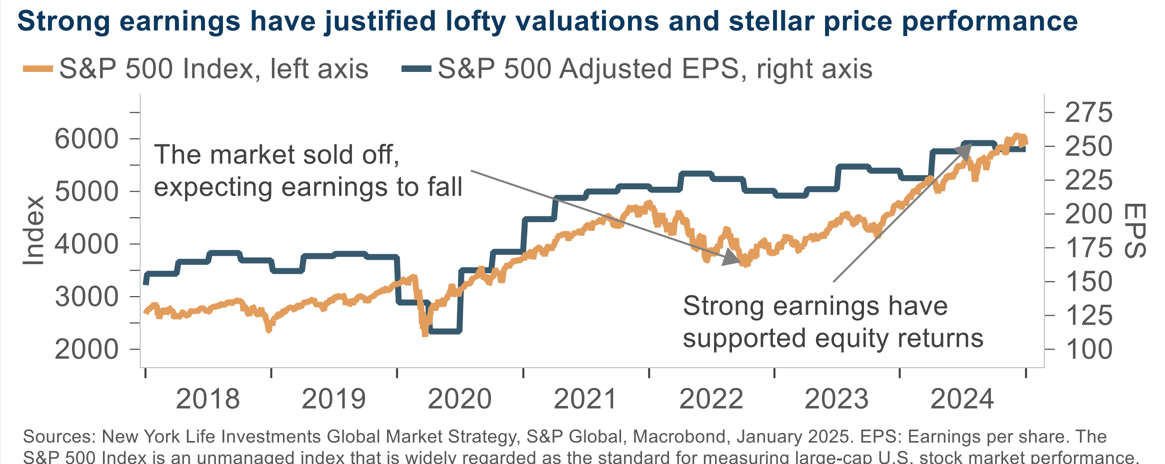
Corporate earnings have been resilient in the face of growing risks

Earnings growth has held up, but cooling demand and still-high costs make the market's 10% earnings growth expectation challenging in our view

Corporate profit margins are the next domino to fall: they may appear resilient but there is a wide dispersion between sectors

Sources: New York Life Investments Global Market Strategy, NBER (National Bureau of Economic Research), Macrobond, January 2025.

Strong earnings have justified lofty valuations and stellar price performance



Sources: New York Life Investments Global Market Strategy, S&P Global, Macrobond, January 2025. EPS: Earnings per share. The S&P 500 Index is an unmanaged index that is widely regarded as the standard for measuring large-cap U.S. stock market performance. It is not possible to invest in an index. Past performance is not a guarantee of future results.

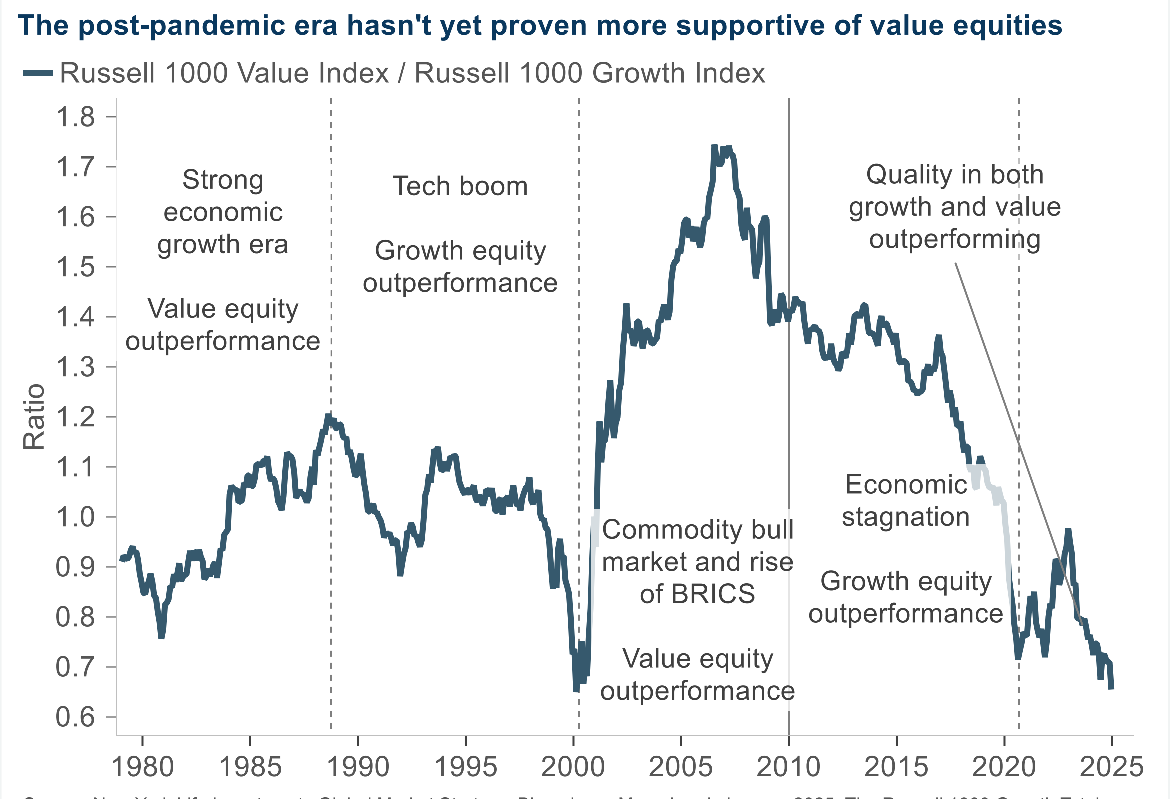
- Equity markets are priced based on earnings and multiple expansion (or contraction), with multiples being influenced by factors such as cost of capital and investor sentiment.
- Corporate earnings have remained resilient in the face of increasing risks. Profit margins appear resilient (**left chart**) but there is a wide dispersion between sectors with tech seeing the most strength. Today, the market is still optimistic about earnings growth. Market pricing suggests earnings per share (EPS) are expected to grow by 10% in 2024 and 15% in 2025. For context, EPS nudged up by only 0.5% in 2023 – a period of very strong economic activity – and 5.0% in 2022. From our perspective, achieving a much higher level of earnings growth this year would require economic growth to accelerate meaningfully, a development we don't see as likely or lasting.
- How much of a selloff should investors expect if earnings growth came into question? In a typical earnings-related selloff, based on the past 16 recessions (excluding the Covid recession), the median draw down in real EPS is 21%. In 2022, the S&P 500 experienced an 25% drawdown when investors began to doubt corporate resilience (**right chart**). But in this case, performance rebounded - profits were ultimately boosted by business and wage supports, as well as lower rates locked in from the years of easy monetary policy. If earnings don't expand further from here, investors hoping for higher equity valuations would be left to rely on multiple expansion via falling rates and improving confidence.

TAKEAWAY: Stable corporate earnings have provided support for equity performance; however, inflation and margin compression remain a risk for many of these companies. Investors are pricing in strong earnings growth, but we remain cautious as late cycle dynamics could quickly shift investors' outlooks.

Growth equity outperformance continues but remains the "pain trade"

A fear of missing out appears to be driving growth outperformance despite more compelling fundamentals in value equities

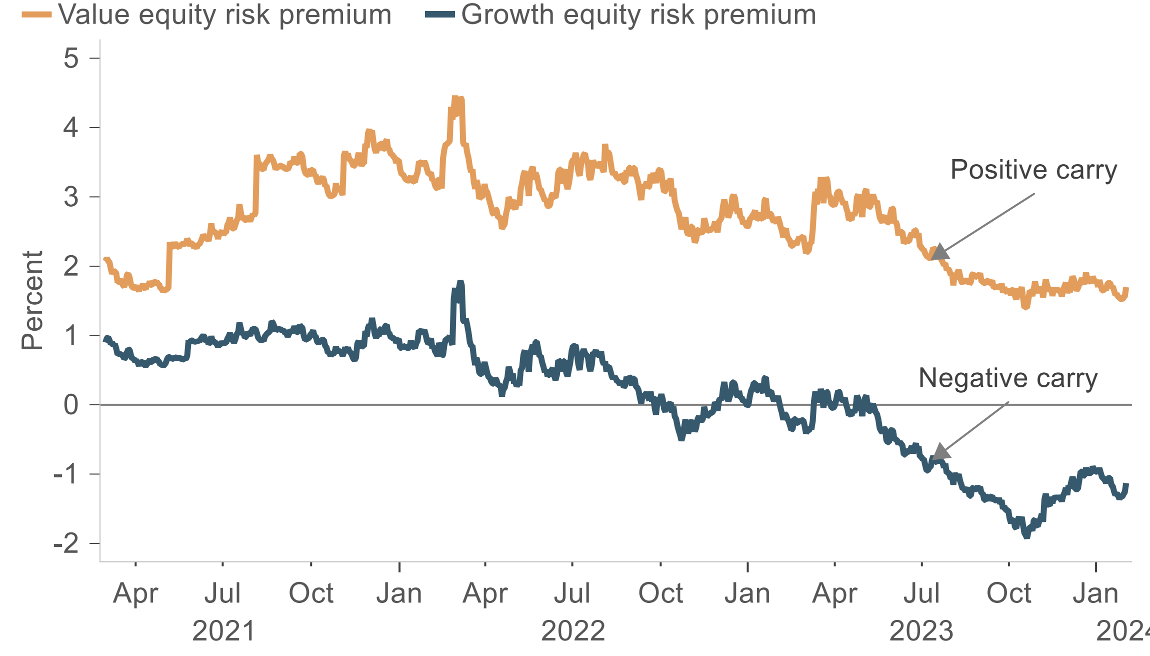
The post-pandemic era hasn't yet proven more supportive of value equities



Source: New York Life Investments Global Market Strategy, Bloomberg, Macrobond, January 2025. The Russell 1000 Growth Total Return Index measures the performance of large-cap growth-oriented stocks in the U.S. market. The Russell 1000 Value Total Return Index measures the performance of large-cap value-oriented stocks in the U.S. market. It is not possible to invest in an index. Past performance is not a gaurantee of future results.

Value equities offer positive carry, growth equities appear overbought

Equity risk premium represents the index's expected earnings yield less the U.S. 10-year Treasury yield.



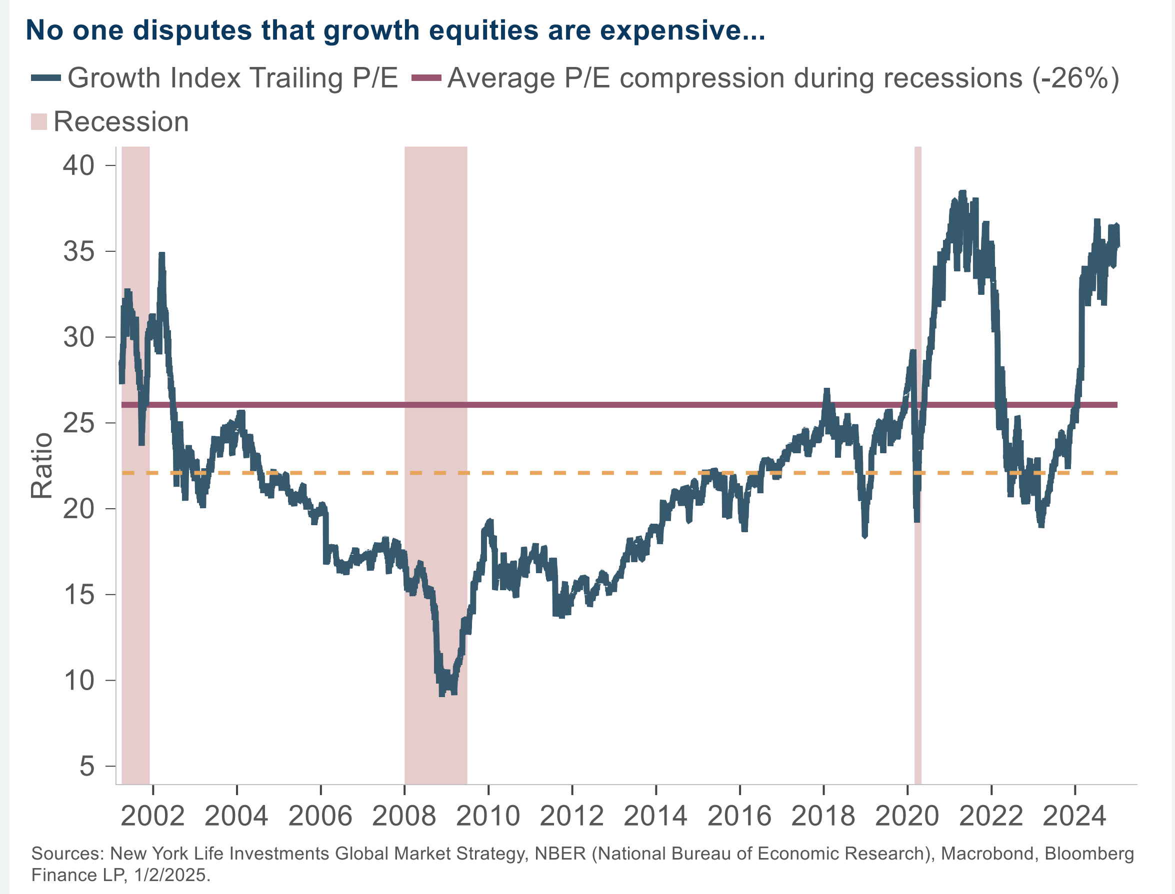
Source: New York Life Investments Global Market Strategy, U.S. Treasury, Bloomberg, Macrobond, January 2025. Value is represented by the Russell 3000 Value Index, which measures the performance of value-oriented stocks in the U.S. market. Growth is represented by the Russell 3000 Growth Index, which measures the performance of growth-oriented stocks in the U.S. market. Past performance is not a guarantee of future results.

TAKEAWAY: Growth equity is likely to maintain its dominance in this late-stage cycle and in the case of recession in our opinion. The following slides will look under the hood of valuations and fundamentals among growth and value equities.

Growth vs value: classic valuation divergence creates opportunities

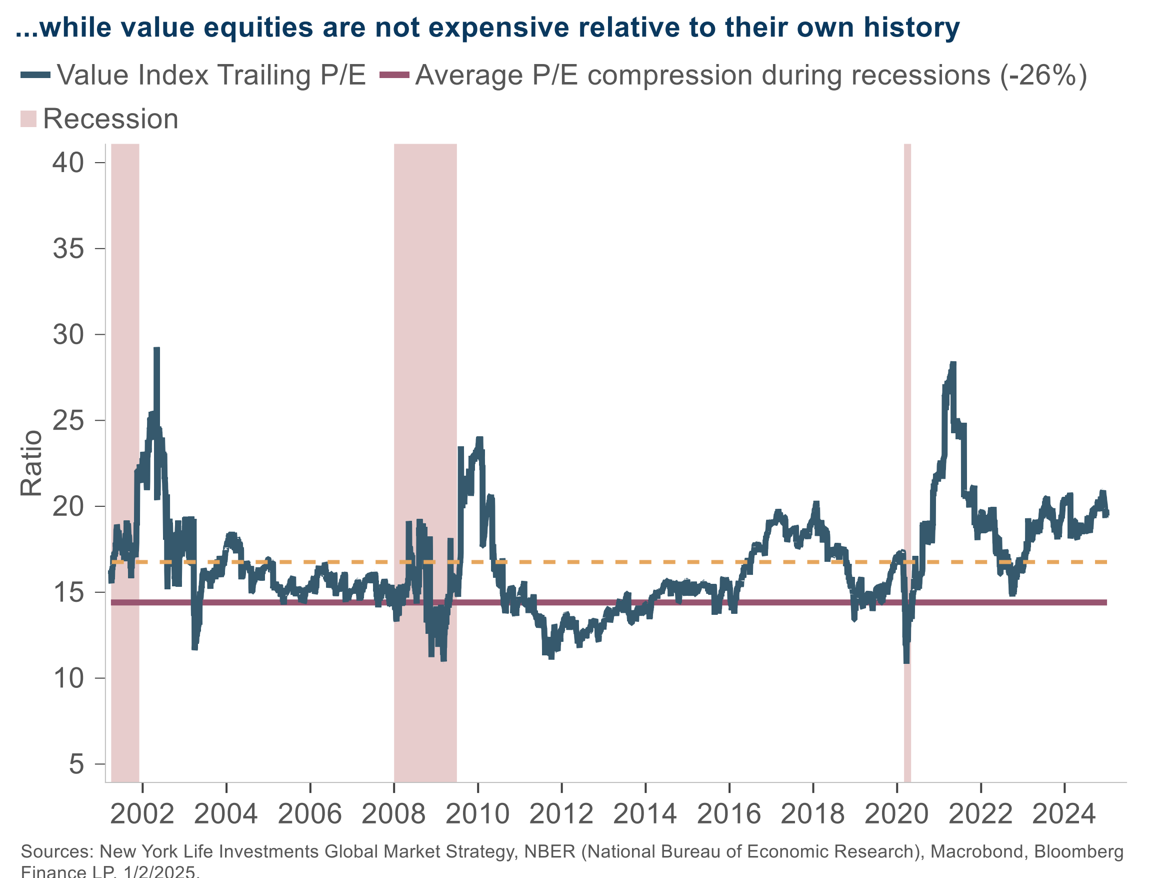
Valuation-sensitive investors can seek relative shelter in high quality, large cap value equities

No one disputes that growth equities are expensive...



Sources: New York Life Investments Global Market Strategy, NBER (National Bureau of Economic Research), Macrobond, Bloomberg Finance LP, 1/2/2025.

...while value equities are not expensive relative to their own history



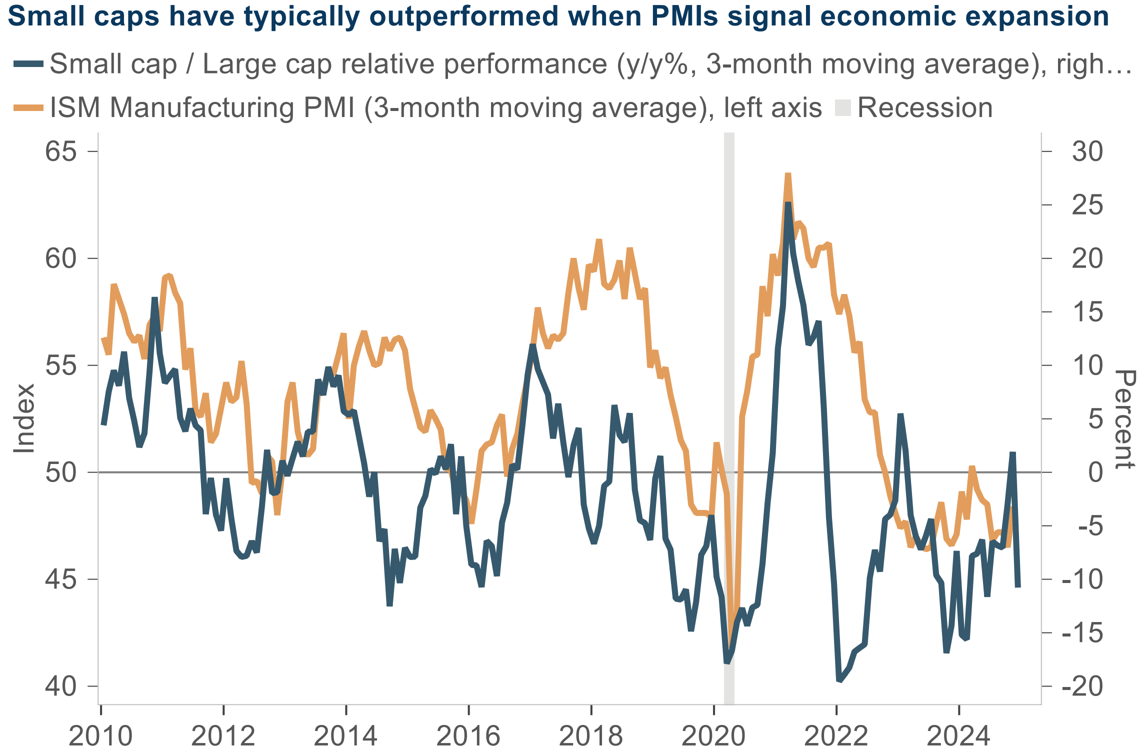
Sources: New York Life Investments Global Market Strategy, NBER (National Bureau of Economic Research), Macrobond, Bloomberg Finance LP, 1/2/2025.

TAKEAWAY: Within growth equities, we see the most compelling opportunities among managers who can identify growth-at-a-reasonable price (also known as GARP investing) with strong market positions and healthy financials. Value equity provides a valuation and carry opportunity, but may not see expansion until the economic cycle re-accelerates.

Large caps are likely to outperform as U.S. economic risks rise

However, we also maintain some small cap exposure, especially where we see structural opportunity linked to artificial intelligence

Small caps have typically outperformed when PMIs signal economic expansion



Sources: New York Life Investments Global Market Strategy, Institute for Supply Management (ISM), Russell Investment Group, S&P Global, NBER (National Bureau of Economic Research), Macrobond, January 2025. Small caps are represented by the Russell 2000. Large caps are represented by the S&P 500. The Russell 2000 is a market index that measures the performance of 2,000 small, public companies in the U.S. The S&P 500 Index is an unmanaged index that is widely regarded as the standard for measuring large-cap U.S. stock market performance. Past performance is not a guarantee of future results. It is not possible to invest in an index.

- The equity market recovery from December 2022 has been driven by large cap tech stocks. We expect this to continue as U.S. economic activity slows and investors favor the historical resiliency of large companies.
- Large cap equities tend to hold less floating-rate debt than small caps do, which is why they have outperformed as interest rates have risen.

When should I buy small caps?

- It's primarily about the cycle: small cap outperformance typically occurs when the economy is rebounding, unemployment is falling, and corporate earnings growth is strong.
- Small cap outperformance, defined as the small cap/large cap ratio moving up, typically tracks the ISM Manufacturing PMI, a proxy for economic growth (**chart**).
- On the whole, we would only expect small caps to recover if the U.S. economy were to reaccelerate.
- However, small caps saw a sharp rebound recently following the July inflation release, demonstrating the potential benefits of diversification. Though we believe the market's "soft landing" assumptions are liable to shift, the path is always bumpy and some diversification can be valuable.

Small caps may offer overlooked growth opportunities

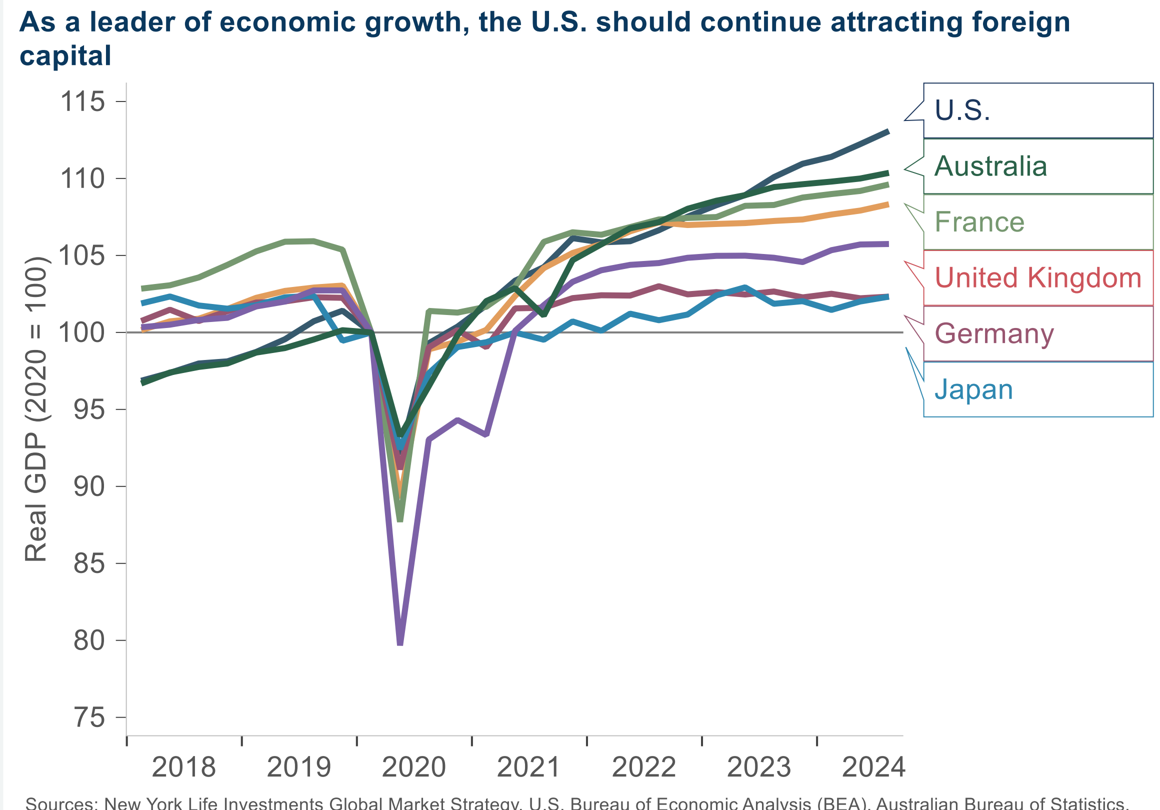
- Within the asset class, we think there are pockets of opportunity where investors can capitalize on structural themes like the building-out of artificial intelligence (AI).
- Small and medium-sized profitable growth companies, for instance, may offer exposure to artificial intelligence development at attractive valuations.

TAKEAWAY: As the market narrative shifts between recession and inflation, the outlook for small caps is dim in our opinion. Small caps have typically underperformed during slowdowns and amid rising prices. Therefore, we aren't overly bullish on small caps until the market narrative shifts to one of economic recovery. Nevertheless, we believe the asset class offers overlooked growth potential, especially those companies with exposure to the artificial intelligence boom and profitable technology.

International equities: relative underperformance during risk-off

While an economic deceleration favors U.S. equities relative to international, we are cautious of a structural international underweight

As a leader of economic growth, the U.S. should continue attracting foreign capital



Sources: New York Life Investments Global Market Strategy, U.S. Bureau of Economic Analysis (BEA), Australian Bureau of Statistics, Statistics Canada, Eurostat, French National Institute of Statistics & Economic Studies (INSEE), German Federal Statistical Office (Statistisches Bundesamt), Japanese Cabinet Office (CAO), Bank of Korea (BOK), U.K. Office for National Statistics (ONS), Macrobond, January 2025.

A cyclical, not structural underweight during recessions

- Many investors are structurally under allocated to international equities, limiting the potential of this asset class to provide sector and business cycle diversification.
- On a cyclical basis, however, we see headwinds. International equities have historically outperformed in times of strong global economic growth and ample liquidity so the current backdrop may not provide much support.
- Idiosyncratic factors also contribute to our slight underweight view for international equities, including political uncertainty keeping investors cautious on European equities, and economic volatility in Japan caused by the normalization of policy – including interest rate hikes.
- When comparing real GDP growth, the U.S. has recovered more than its developed market peers which should continue attracting foreign capital (**chart**).
- In conventional portfolio allocation, international equities make up roughly one-third of total equity exposure. So, in a standard 60/40 portfolio comprised of 60% equities and 40% bonds, international equities would constitute 20% of the portfolio.

Across cycles, international equities offer investors the opportunity to capture sector and business cycle diversification

- Sectors: The S&P 500 is overweight the technology and communications sectors. Europe and Japan have more exposure to cyclical sectors like industrials and consumer discretionary. Relative valuations, especially in Europe, remain attractive for bottom-up stock picking.
- Cycle: Because the global economic cycle is desynchronized, a diversified international exposure can help investors capture recovery cycles globally.

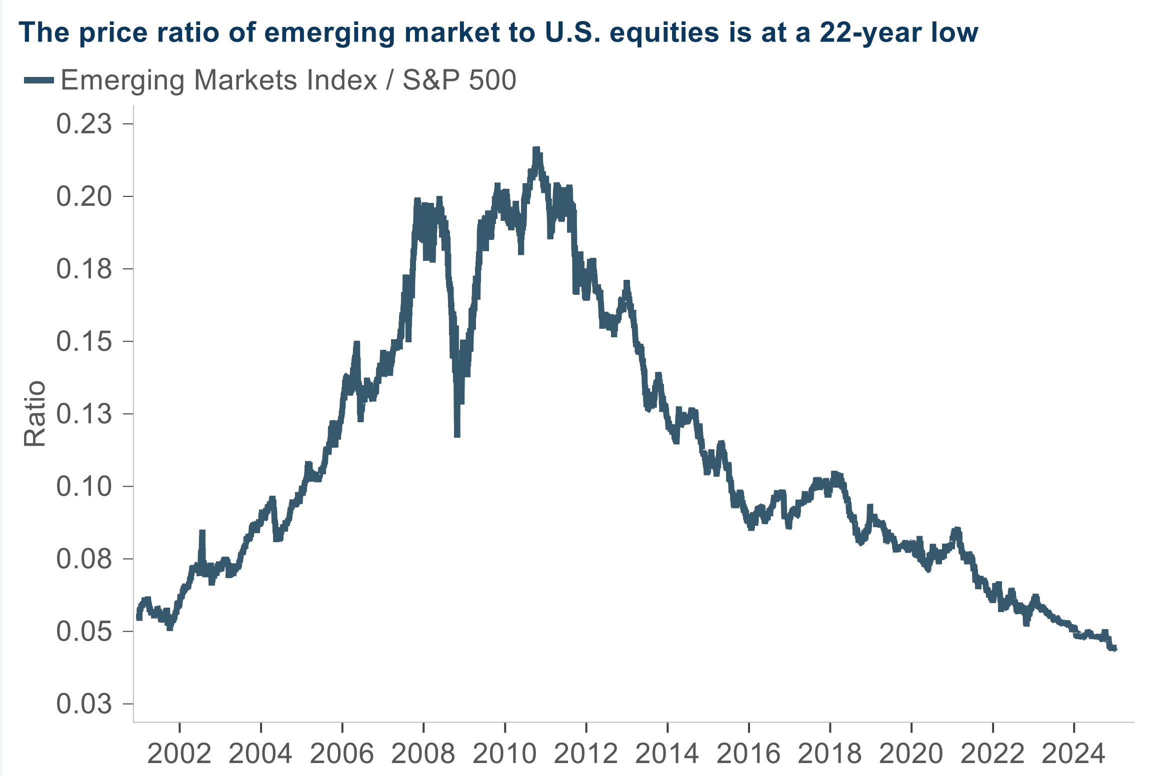
TAKEAWAY: While U.S. equities have been leading in recent months, we believe that structural exposure to international equity can help investors to capture sector and business cycle diversification. Tactically, we remain cautious as the global slowdown will likely see U.S. equities outperform non-U.S. equities.

Investments

Emerging market equities may still struggle against gravity

Some markets stand out, but the asset class may have difficulty outperforming as global growth slows

The price ratio of emerging market to U.S. equities is at a 22-year low



Sources: New York Life Investments Global Market Strategy, S&P Global, Macrobond, January 2025. The S&P 500 is an unmanaged index that is widely regarded as the standard for measuring large-cap U.S. stock market performance. Emerging Markets index is represente by the MSCI Emerging Markets Index. The MSCI Emerging Markets Index is a free-float weighted equity index that captures large and mid cap representation across Emerging Markets (EM) countries. It is not possible to invest in an index. Past performance is no guarantee of future results.

EM equity outperformance may be difficult with China weighing down the index

Sources: New York Life Investments Global Market Strategy, Bloomberg, Macrobond, January 2025. Emerging Market index is represented by the MSCI Emerging Markets Index. The MSCI Emerging Markets Index is a free-float weighted equity index that captures large and mid cap companies across EM countries. Emerging Markets ex China index is represented by the MSCI EM ex China which excludes China from the MSCI EM index. It is not possible to invest in an index. Past performance is no guarantee of future results.

- Emerging market (EM) central banks led the cycle on raising rates and some have now begun an easing cycle suggesting the potential for more monetary support in these markets.
- EM equities have generally underperformed U.S. equities since 2012. We believe investors are under-allocated to EM equities, so a shift in investor sentiment could have a significant impact (**left chart**).
- China's economic performance remains a risk for EMs, at least until we see an end to its cyclical slowdown (**right chart**).

TAKEAWAY: With U.S. interest rates likely peaked, EM equities may see greater interest in 2025; nevertheless, we expect currency hedging and active management are key for success in the asset class

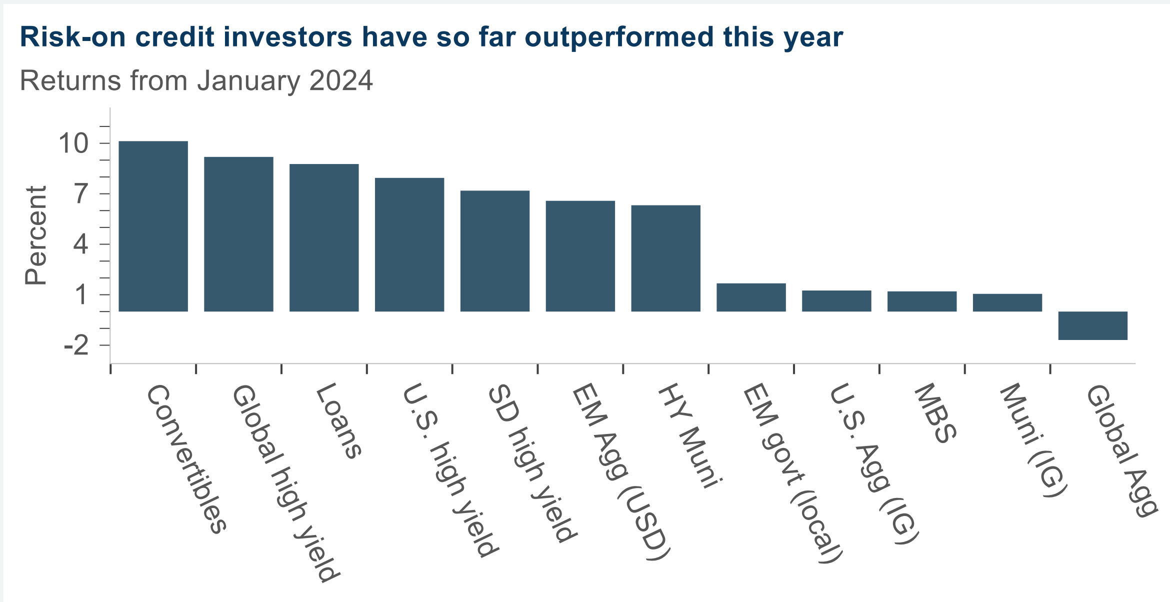
Credit remains appealing as the Fed cuts

Tight credit spreads limit price appreciation, but good credit quality and still-attractive yields make overweight credit one of our highest convictions

- Resilient growth and moderating inflation have prompted yield curve normalization after its two-year inversion. This historically drives a supportive environment for credit assets. Our credit managers point to a potentially "goldilocks" scenario in which slightly lower rates improve borrower conditions without sacrificing strong income generation potential.
- What about spreads? A sharp policy easing in response to a growth downturn or weaker labor market would likely drive spread widening. However, structurally stronger credit quality, a favorable economic backdrop, and still-strong income generation potential make us confident in credit allocation.
- Given near-term Treasury supply uncertainty, duration is not our favorite place to take risk. We prefer short duration corporate credit exposure, with long duration in the municipal bond curve where such risk is better rewarded in our view.

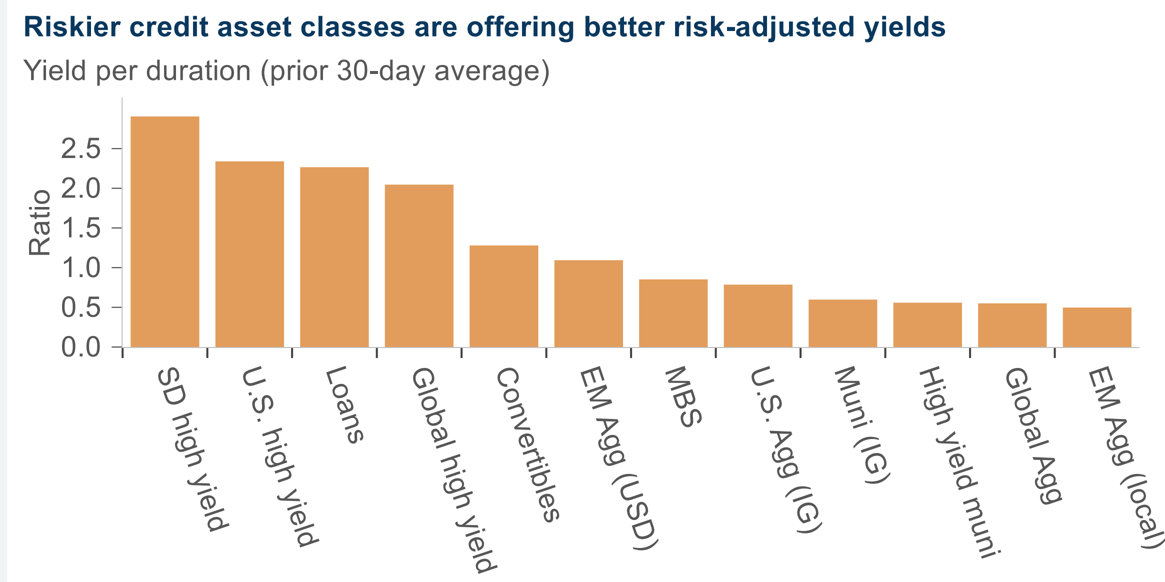
Risk-on credit investors have so far outperformed this year

Returns from January 2024



Riskier credit asset classes are offering better risk-adjusted yields

Yield per duration (prior 30-day average)

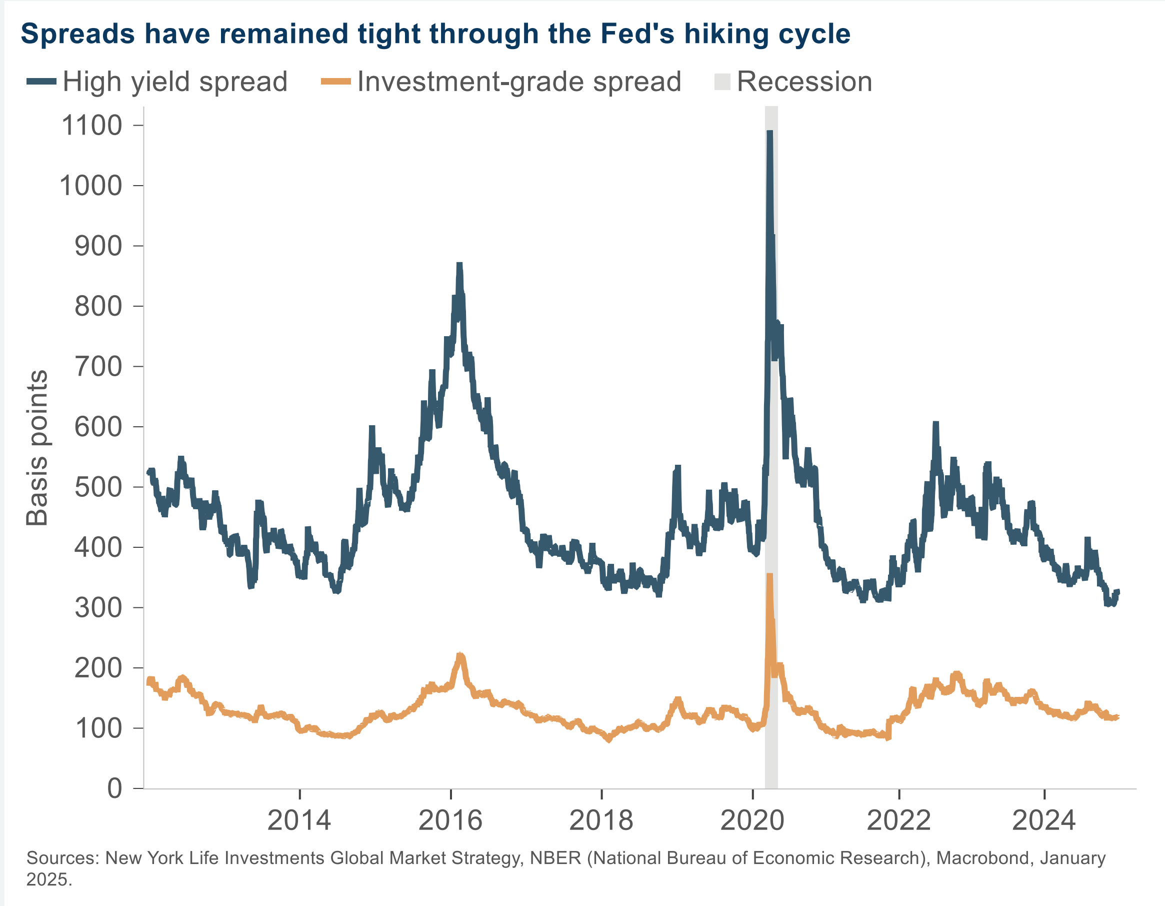


Sources: New York Life Investments Global Market Strategy, Bloomberg, Macrobond, January 2025. Convertibles represents the Bloomberg U.S. Convertibles Liquid Bond Index. EM Agg represents the Bloomberg Emerging Markets (EM) Hard Currency Aggregate Index- a flagship hard currency EM debt benchmark. EM govt represents the Bloomberg Emerging Markets Local Currency Government Index-a flagship index that measures the performance of local currency Emerging Markets (EM) debt. Global Agg represents the Bloomberg Global Aggregate Index- a flagship measure of global investment grade debt. Global high yield represents the Bloomberg Global High Yield Index-a measure of the global high yield debt market. Loans represents the Bloomberg US Leveraged Loan Index-measures the institutional leveraged loan market. Muni represents the Bloomberg U.S. Municipal Index-covers the long-term tax-exempt bond market. U.S. Agg represents the Bloomberg US Aggregate Index-a broad-based benchmark that measures the investment grade bond market. U.S. high yield represents the iBoxx USD Liquid High Yield Total Return Index-measures the sub-investment grade, corporate bond market. U.S. MBS represents the Bloomberg US Mortgage Backed Securities (MBS) Index-tracks agency mortgage backed pass-through securities. U.S. high yield muni represents the Bloomberg Muni High Yield Total Return Index. Short duration (SD) high yield represents the Bloomberg US High Yield Ba/B 1% Cap 1-5 Year TR Index. It is not possible to invest in an index. Past performance is not a guarantee of future results.

Flows into investment-grade bonds could rise as the economy slows

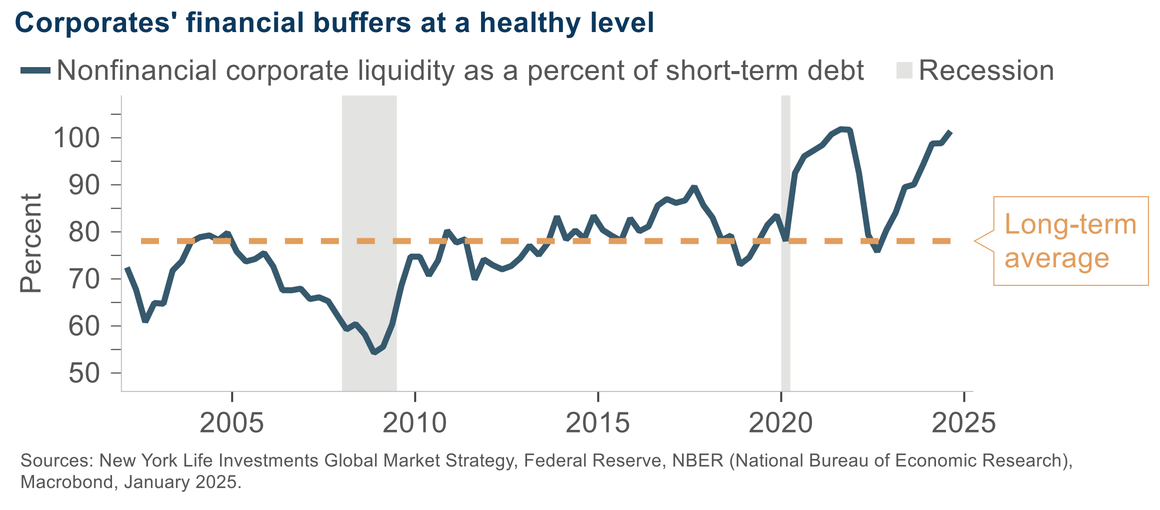
Given our late cycle view of the economy, we do not believe there is room for spreads to tighten, but yields remain attractive

Spreads have remained tight through the Fed's hiking cycle



Sources: New York Life Investments Global Market Strategy, NBER (National Bureau of Economic Research), Macrobond, January 2025.

Corporates' financial buffers at a healthy level



Sources: New York Life Investments Global Market Strategy, Federal Reserve, NBER (National Bureau of Economic Research), Macrobond, January 2025.

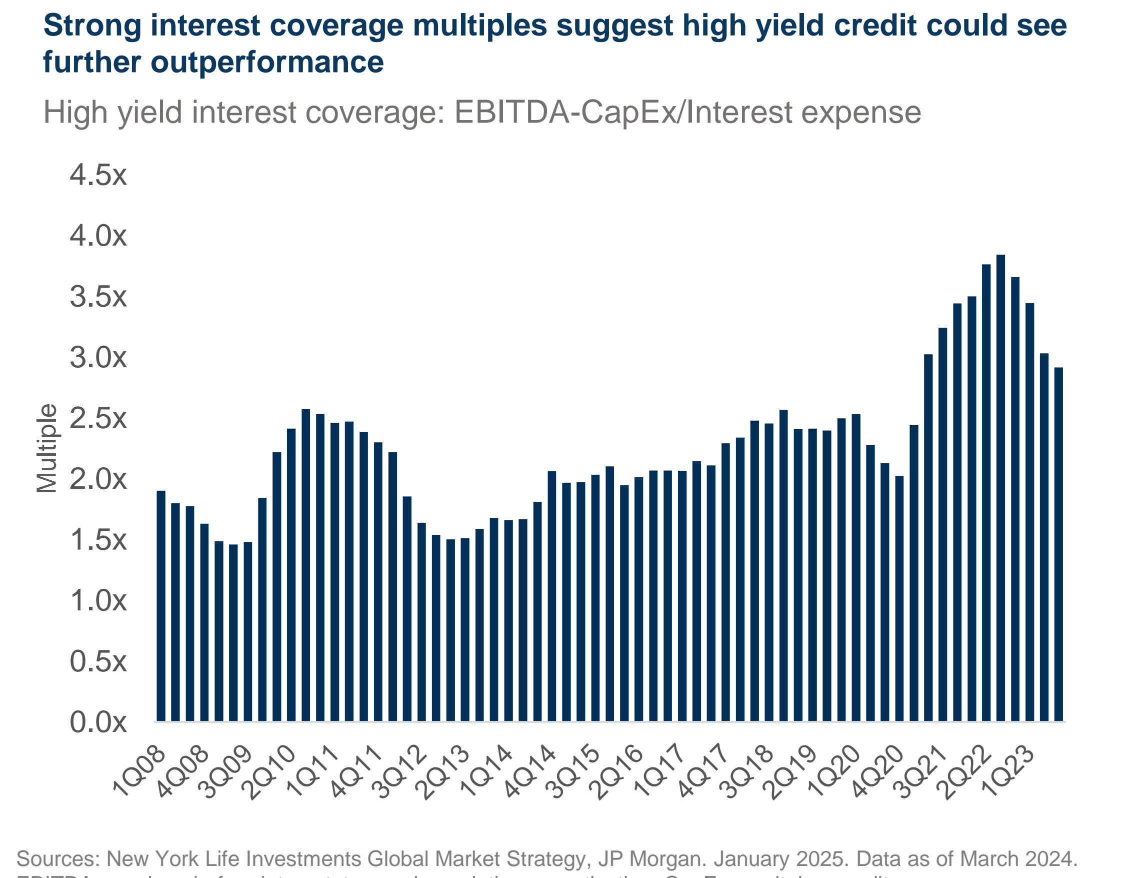
- Credit spreads have remained remarkably tight as the Fed embarked on its rate hiking cycle (**left chart**). The tight spreads could be attributed to (1) a buildup of cash and (2) the concentration of investment grade and high yield issuers is biased towards consumer sectors which have been especially strong this cycle due to fiscal supports.
- Businesses are maintaining a healthy cash balance (**right chart**), which should help firms weather shrinking margins and higher interest expenses
- This economic environment underscores the importance of discerning borrowers' adaptability to slower growth and a prolonged period of high inflation and interest rates, which may require an active and dynamic approach to security selection.

TAKEAWAY: Since the pandemic, companies have increasingly adopted a conservative approach to managing their balance sheets, effectively limiting overall debt growth. We believe this trend has created an attractive backdrop for investment-grade corporate bonds. While we expect credit spreads to widen as the economy weakens and rate volatility rises, given improvements in credit quality, we may not see the same spikes we've seen in past cycles.

U.S. high yield is remains one of our highest conviction ideas

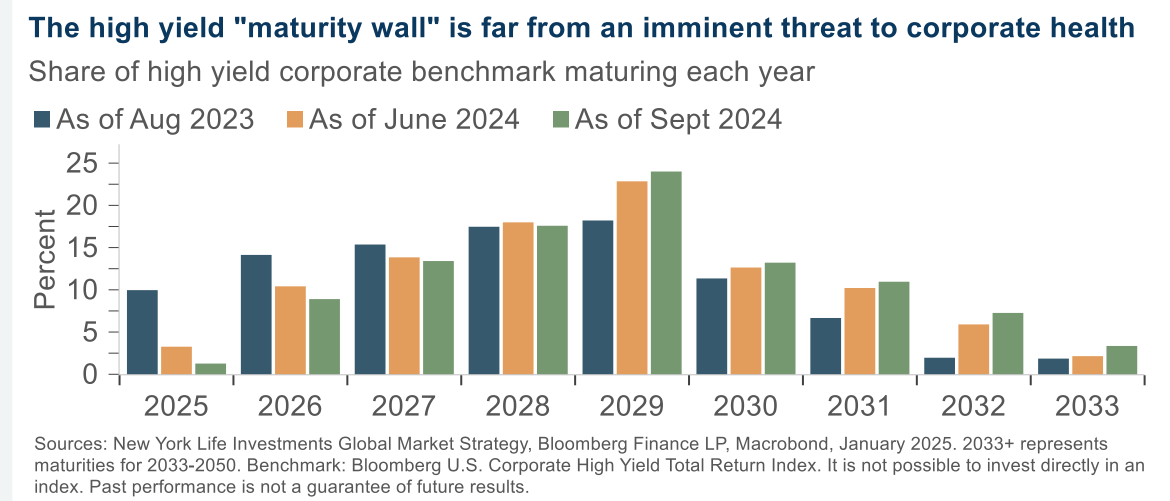
We maintain a positive outlook on U.S. high yield credit, supported by attractive pricing, quality, and a favorable maturity schedule

Strong interest coverage multiples suggest high yield credit could see further outperformance



Sources: New York Life Investments Global Market Strategy, JP Morgan. January 2025. Data as of March 2024. EBITDA: earnings before interest, taxes, depreciation, amortization; CapEx: capital expenditures.

The high yield "maturity wall" is far from an imminent threat to corporate health



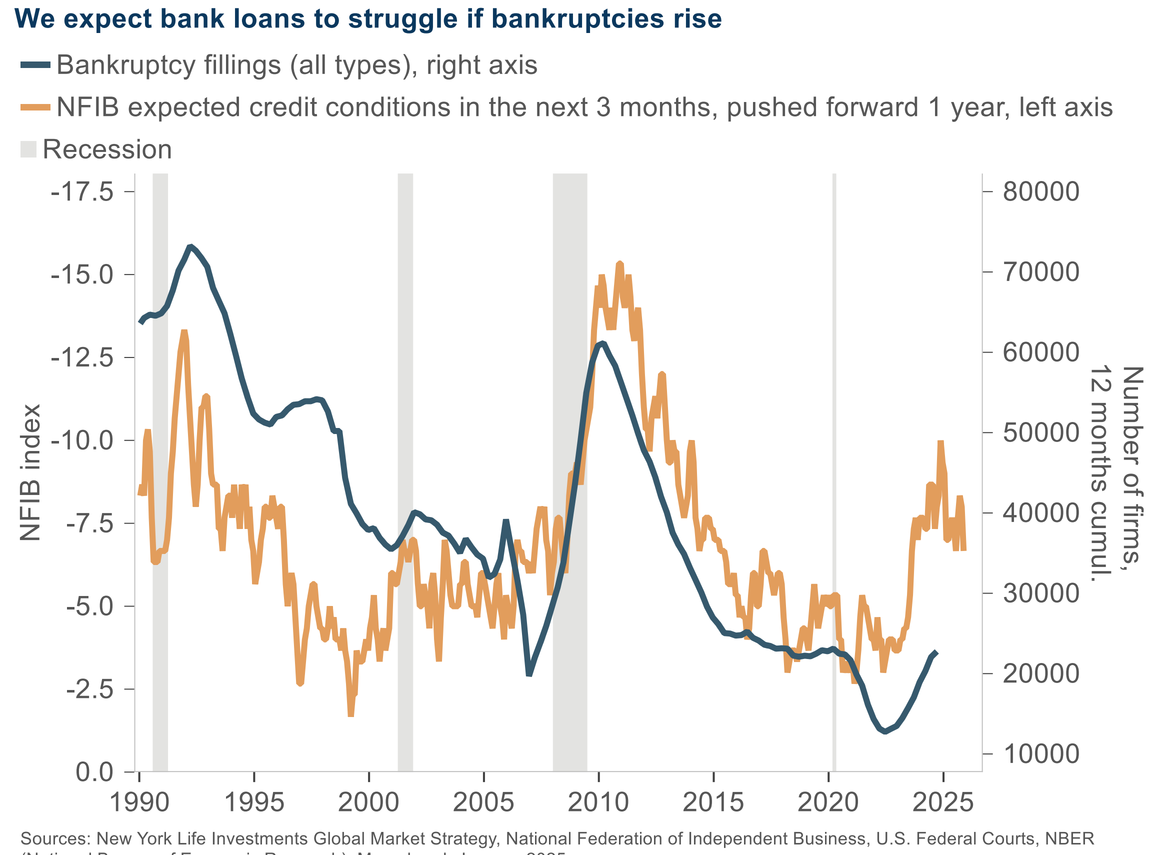
Sources: New York Life Investments Global Market Strategy, Bloomberg Finance LP, Macrobond, January 2025. 2033+ represents maturities for 2033-2050. Benchmark: Bloomberg U.S. Corporate High Yield Total Return Index. It is not possible to invest directly in an index. Past performance is not a guarantee of future results.

- Both high yield leverage and interest expense are at healthy levels (**left chart**). So far this year, the lower-rated subsets of the credit market have outperformed and could continue to as the Fed eases policy. That said, issuer selectively will remain key.
- Over half of major benchmark weight is now rated BB or higher. We see this quality at work in the maturity wall: high yield issuers in the U.S. have been incredibly successful at pushing out their obligations (**right chart**).
- The U.S. high yield asset class has improved in quality thanks to pandemic-era programs as well as changes in corporate financing structure in the post-financial crisis period.

TAKEAWAY: High yield is not typically an asset class investors hold as economic risks rise, but we believe high quality, high yield borrowers could provide significant value in a portfolio this year. For investors concerned about equity volatility, high yield corporate bonds have a better risk/reward offering compared to equities over the last 12 months.

Bank loans may still have more room to run

Investors continue to favor leveraged loans for their attractive higher yields



Sources: New York Life Investments Global Market Strategy, National Federation of Independent Business, U.S. Federal Courts, NBER (National Bureau of Economic Research), Macrobond, January 2025.

Bank loans when the Fed is cutting?

- Yes, rate cuts can be constructive outside of a recession as they ease pressure off borrowers which supports fundamentals and stable CLO demand
- Bank loans could have a good 6 months or so from an allocation perspective since overall yields are still higher than other comparable asset classes.

Positive outlook

- Leveraged loans currently have better carry relative to bonds and issuance (~$130bn YTD), a proxy for loan demand, remains supportive of loan technicals.
- While the asset class saw a strong 2023, slower growth presents a risk. Worsening credit conditions (**chart**) seen in the orange line rising are typically followed by a rise in bankruptcy filings (blue line rising).
- However, on a more positive note, S&P Global Ratings expects the leveraged loan index default rate to hover around 1.5% through June 2025 providing a strong backdrop for the asset class.

Portfolio strategy

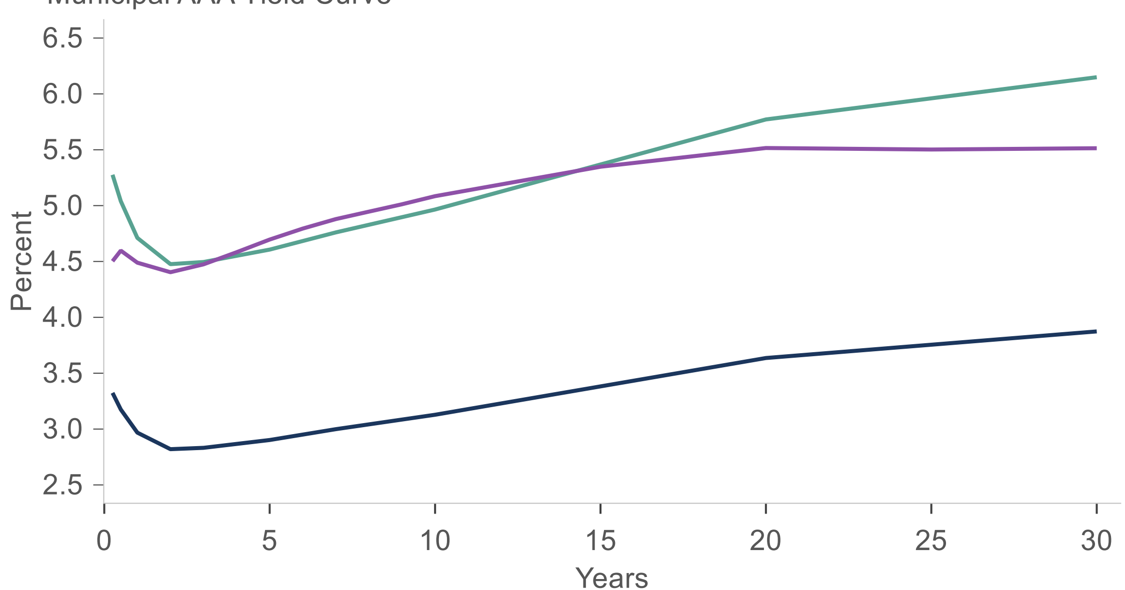
- We believe bank loans are an important component of diversified global bond exposure. Within the asset class, we prefer portfolios that are overweight senior secured loans with low leverage.

TAKEAWAY: At this stage in the cycle, Fed rate cuts are favorable for the asset class, especially given the yield spread relative to other bond types. However, with the risk of an economic slowdown intensifying, we believe bank loan investors should play more defense than offense at this point..

Munis provide a diversified approach to credit and duration exposure

Strong credit fundamentals, rising tax burden, and higher yields make municipal bonds an attractive credit diversifier in our view

Muni's tax equivalent yields exceeds AAA corporates' at longer durations



Sources: New York Life Investments Global Market Strategy, U.S. Department of Treasury, Macrobond, January 2025. The AAA corporate yield curve is populated with USD denominated senior unsecured fixed rate bonds issued by U.S. companies with a rating of AA+ , AA or AA-. The Municipal AAA yield curve is populated with high quality U.S. municipal bonds with an average rating of AAA from Moody's and S&P. The tax-equivalent yield curve assumes a 37% tax rate. Duration of fixed income securities is a measure of a security's price sensitivity to changes in interest rates, measured in years.

Tailwinds & outlook for municipal bonds

- Like corporate bond issuers, municipalities are also well capitalized with healthy reserve balances. This strong starting point provides a needed cushion should revenues and federal aid decline. This also implies that, due to economic uncertainty, issuance is not expected to pick up in 2025.
- Tax burdens are rising due the increase in federal support to businesses and individuals, combined with a robust housing market driving elevated property tax valuations. Additionally, the expanding federal deficit could result in higher federal tax rates, making tax-exempt income even more attractive. Further, the benefit of tax-exemption is amplified in the current "higher for longer" yield environment.
- Our outlook for the asset class is positive. This year muni investors seem to be recognizing the benefits of locking in tax-exempt income at these rates, while exhibiting less anxiety over inflation, and less confidence in money market/cash yields maintaining their levels.

Tactical view on municipal bond exposure

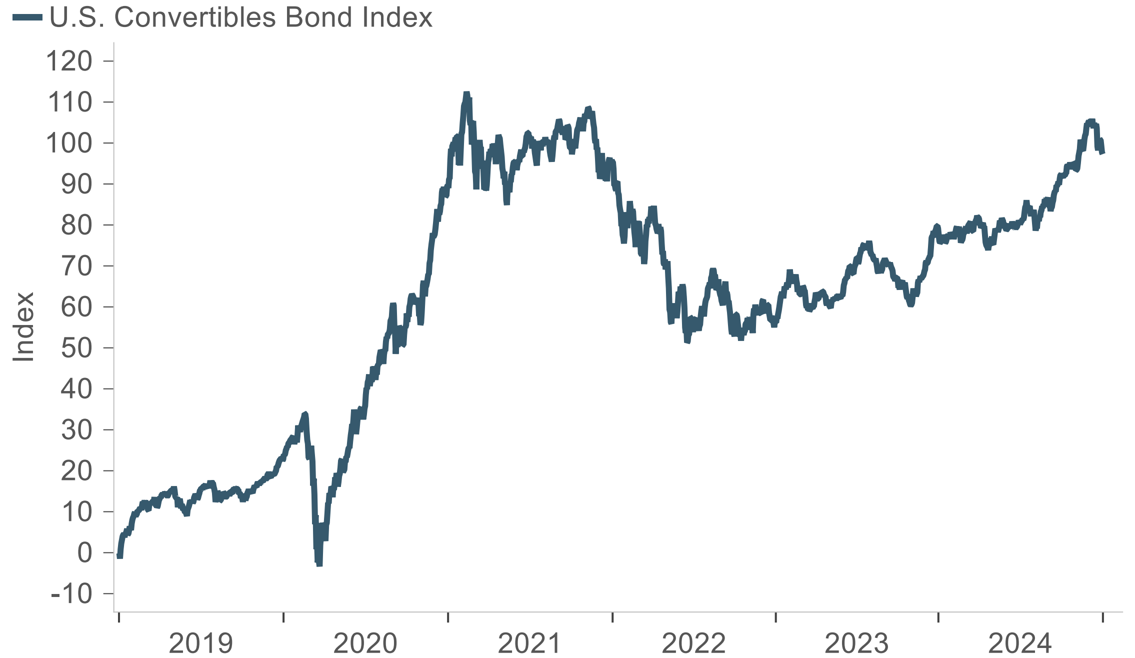
- In our view, an inverted or flat yield curve gives investors little incentive to take excessive risk in duration in U.S. Treasuries; however, not all duration is created equal. The municipal curve remains upward sloping which continues to compensate investors for longer-term risk while the U.S. Treasury curve remains inverted (**chart**). Tax-free municipal bonds can also balance shorter-duration allocations in the money market or high yield corporate bonds.
- We also like *taxable* municipal bonds as a duration-balancing, long-infrastructure play. Higher credit quality and diversified credit exposure provide additional benefits to this portfolio construction technique, in our view.

TAKEAWAY: Instead of adding duration in Treasuries, investors can consider interest rate risk where it pays to like on the municipal bond curve. Additionally, robust fundamentals and a high interest rate environment, plus the risk of higher taxes, create a solid backdrop for municipal bonds.

The tide may be turning in favor of convertible bonds

Convertible bonds are well positioned to hedge downside risk while offering similar upside potential in the event of a broad market rebound

The lack of U.S. mega-cap companies within the convertible bond sector has limited upside. But convertible bonds remain an attractive option for portfolio diversification.



Sources: New York Life Investments Global Market Strategy, Bloomberg, Macrobond, January 2025. Convertible securities index is represented by the Bloomberg U.S. Convertibles Liquid Bond Index. The Bloomberg U.S. Convertibles Liquid Bond Index tracks the performance of the liquid segment of the U.S. convertible bonds market, on a total return basis, without any adjustments for currency hedging.

What makes convertible bonds special?

- Much like equities, convertible bonds offer unlimited upside potential from the embedded call option on the issuer's common stock, and rate-risk protection from the bond features
- Most convertible bonds have a short duration of approximately 2-3 years, limiting their sensitivity to interest rate fluctuations.
- Over a complete market cycle, convertibles generally participate in about 60-80% of equity market upside and 50% of the downside.

Tactical market outlook:

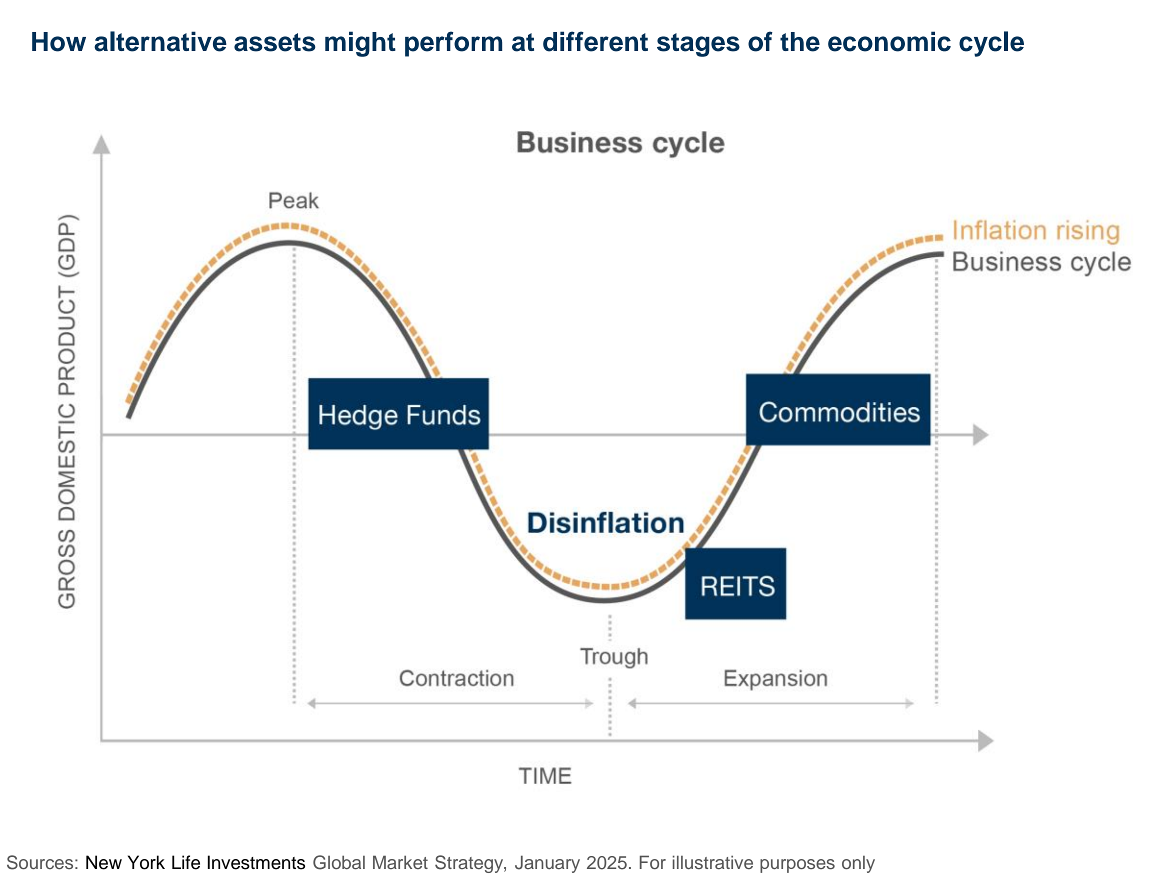
- Issuance: Issuance was strong in 2024, the market saw $45b of new issuance through August compared to $33b over the same period last year. Issuance is expected to increase as investment grade companies with debt maturing may be drawn to the convertible market as they can no longer issue bonds yielding 2% to 3%.
- Approximately one-quarter of new convertible issuance last year was investment grade, and we expect that trend to continue as investment grade companies may find better funding opportunities in the convertible market..
- Valuation: The U.S. convertible market is weighted towards mid and small-cap companies which now have significantly lower valuations than large caps
- For investors who believe market gains can broaden but the economy is still slowing, convertible bond exposure could replace small- and mid-cap exposure which offer potentially similar risk/return opportunities and the defensive bond features.
- The lack of U.S. mega-cap companies within the convertible bond sector has restrained upside, but convertible bonds remain an attractive option for portfolio diversification (**chart**).

TAKEAWAY: Convertible bonds are a well-positioned defensive asset offering yield and low volatility. As real rates rise, the case for convertible bonds becomes compelling, especially as corporate bond issuers are priced out of the investment grade market.

Alternative investments across the business cycle

Plus, asset weighting recommendations based on quantitative portfolio risk/return analysis

How alternative assets might perform at different stages of the economic cycle



Sources: New York Life Investments Global Market Strategy, January 2025. For illustrative purposes only

- Alternative investments offer diversification potential and are some of the least correlated public and private investment opportunities
- Though potentially less liquid than traditional investments, performance is typically less sensitive to the movements of global markets – instead driven by diverse sources of returns.

How much alternatives exposure do I need:

- A suitable range typically falls between 5% and 25% of a portfolio.

Commodities

- Commodities tend to benefit from sticky and rising inflation and have performed well year-to-date. The asset class exhibits very little correlation to both stocks and bonds making it a solid diversifier and inflation hedge.
- Allocating between 1% and 7% can provide diversification and protection against inflation. Equities should be the primary source of funding this allocation.

Hedge Funds

- Not all hedge fund strategies are created equally. With equity markets rising, equity-oriented strategies like long/short and event-driven could be successful in this environment.
- A range of 1% to 12% allows for exposure to skilled fund managers and unique strategies. Typically, this allocation can potentially be sourced from equities.

REITs

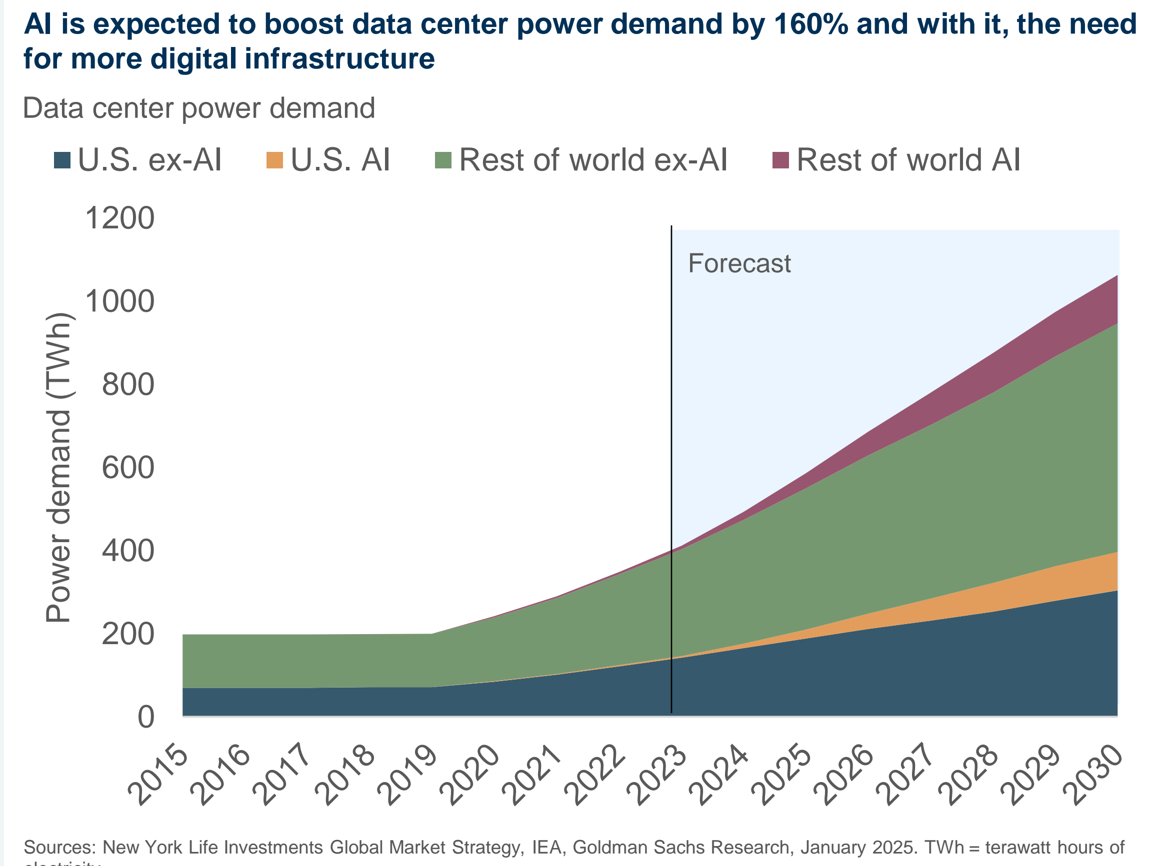
- Concern about commercial real estate has impacted investor sentiment but we think this has the potential to create investment opportunities.
- Allocating between 1% and 15% offers real estate exposure with the potential for income and capital appreciation—and can potentially be sourced primarily from equities.

TAKEAWAY: Given the risk of persistent and rising inflation, we think commodities offer the highest risk-adjusted return potential, though investors could benefit by adding exposure across alternatives.

Infrastructure is one of our highest conviction structural themes

The structural case for infrastructure is expanding just as the cyclical case (lower rates) begins to support the asset class

AI is expected to boost data center power demand by 160% and with it, the need for more digital infrastructure



Sources: New York Life Investments Global Market Strategy, IEA, Goldman Sachs Research, January 2025. TWh = terawatt hours of electricity

A secular investment case for infrastructure

- We see infrastructure as a key beneficiary of secular global investment trends. A changing economic landscape (artificial intelligence), geopolitical trends (U.S.-China competition), and a renewed focus on resource access (after the COVID-19 pandemic) has driven a surge in public and private sector investment in infrastructure. We expect this trend to persist.
- We believe that the supply chains experiencing the most change are those which may benefit the most from investment: digital transition and artificial intelligence, green transition and electrification, and supply chain re-globalization. As a result, we have particularly high conviction around global infrastructure investment with a focus on digital infrastructure, green and brown energy, utilities, and communications.
- Infrastructure projects are increasing funded through the sale of taxable municipal bonds.

Portfolio construction benefits in equity

- Global equity infrastructure may close a frequent investor gap in international exposure.
- The asset class offers inflation protection as cash flows are often linked to inflation, and on the cost side, inflation protection is often written into long-term contracts (**chart**).

Portfolio construction benefits in fixed income

- Issuance of taxable municipal bonds increased in recent years due to the *Tax Cuts & Job Act* of 2017 which limited the issuance of tax-free municipal bonds.
- Investors may be less familiar with taxable municipal bonds, especially outside the U.S. where municipal bonds are less frequently used. We believe this asset class may provide additional means of generating yield, with the benefit of higher quality and diversified credit exposure.
- We also like taxable municipal bonds as a duration-balancing, long-infrastructure play.

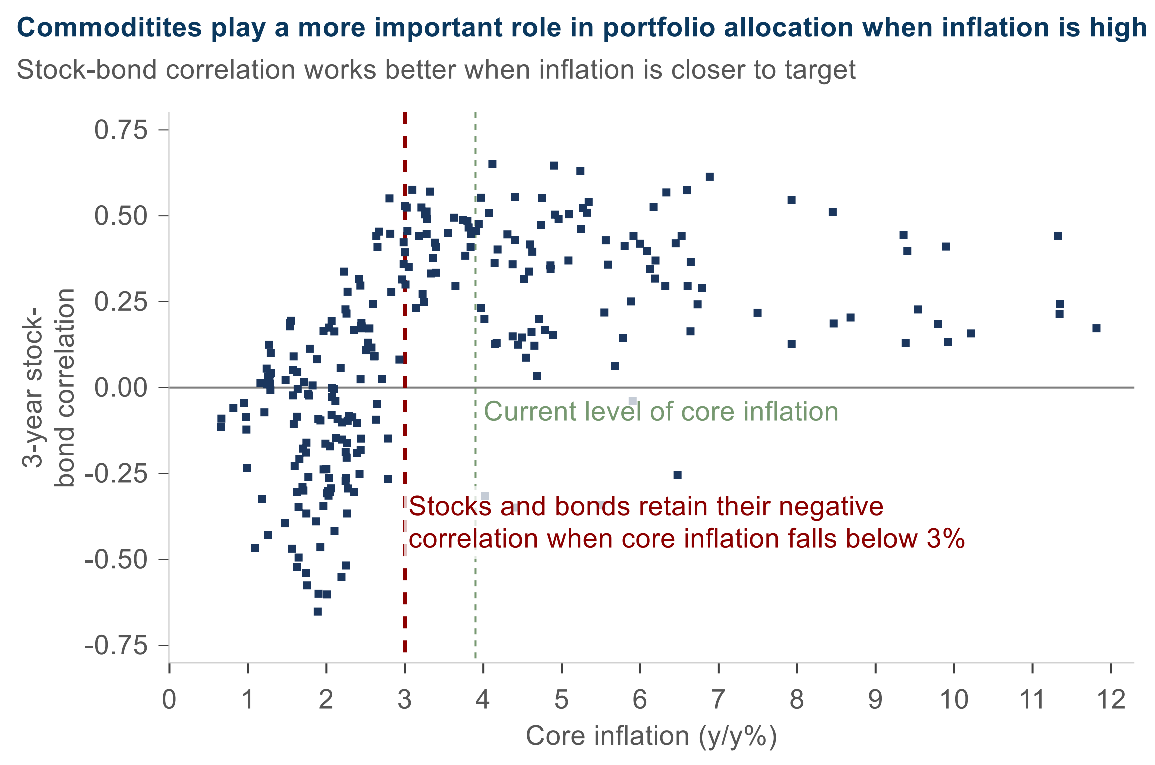
TAKEAWAY: The global economy is shifting, and we believe that infrastructure provides a durable opportunity to capture that change. We perceive infrastructure as a structural allocation in both equity in fixed income, allowing investors access to these trends as well as important portfolio construction benefits. Importantly, an interest rate cutting cycle has historically supported sectors such as utilities and energy that tend to make up important portions of the infrastructure asset class, adding potential cyclical firepower to an already strong structural case in our view.

Higher inflation points to a structural allocation to commodities

Rising demand for resources amid restructuring supply chains provides a compelling investment backdrop for commodities

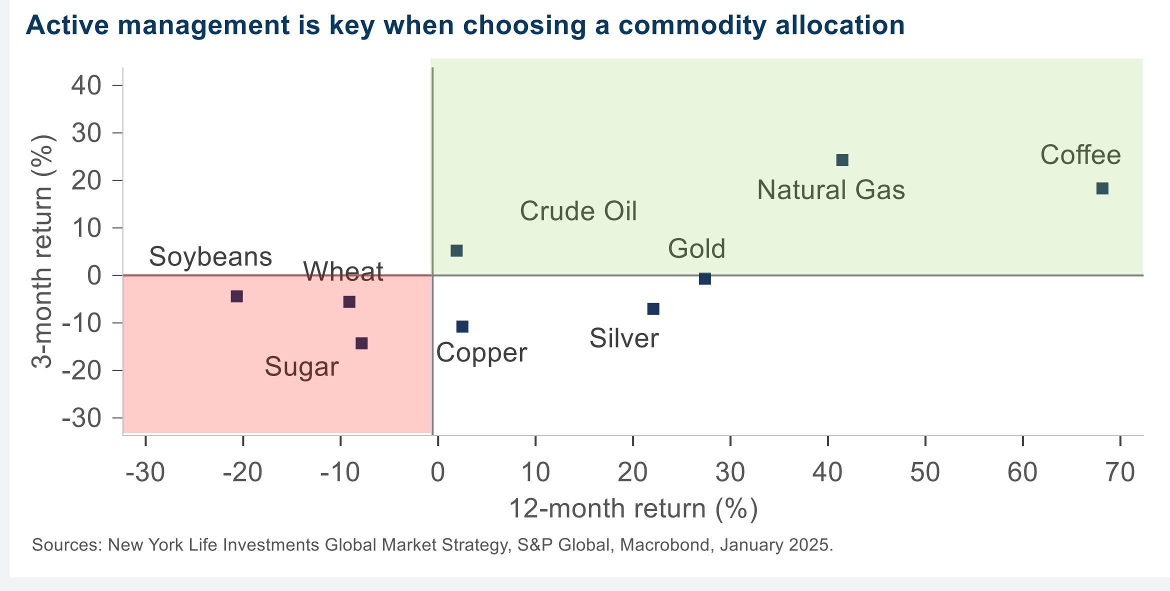
Commoditites play a more important role in portfolio allocation when inflation is high

Stock-bond correlation works better when inflation is closer to target



Sources: New York Life Investments Global Market Strategy, U.S. Bureau of Labor Statistics (BLS), S&P Global, U.S. Department of Treasury, Macrobond, January 2025. Stocks are represented by the S&P 500. Bonds are represented by the monthly return on a U.S. 10-year government bond. Core inflation is represented by the Core CPI index. Core CPI is represented by the core Consumer Price Index. CPI is a measure of the average change over time in the prices paid for a market basket of consumer goods and services. Core CPI excludes volatile food and energy prices. The S&P 500 Index is an unmanaged index that is widely regarded as the standard for measuring large-cap U.S. stock market performance. It is not possible to invest in an index. Past performance is not a guarantee of future results.

Active management is key when choosing a commodity allocation



Sources: New York Life Investments Global Market Strategy, S&P Global, Macrobond, January 2025.

- When inflation is high, stock-bond correlation tends to be higher. Investor portfolios may therefore be less diversified than finance theory would suggest (**left chart**).
- Since the cause of that potentially lower diversification is high inflation, investors could consider increasing their allocation to commodities which may help to manage both risks.
- Not all commodities trade equally (**right chart**); active management can help investors identify commodities with positive momentum (green box) and avoid those with negative momentum (red box)

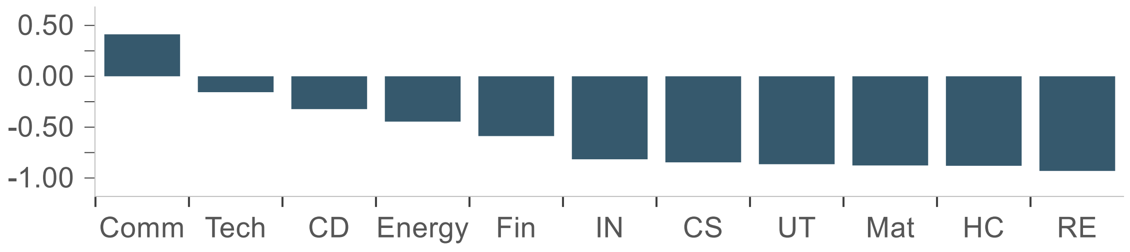
TAKEAWAY: We think investors should consider adding commodities exposure as a hedge against persistent inflation and in response to global dynamics such as escalating trade tensions and the push for decarbonization.

Structural opportunities are opening in liquid real estate

Concern about pockets of commercial real estate, such as office, has impacted investor sentiment, creating potential opportunities

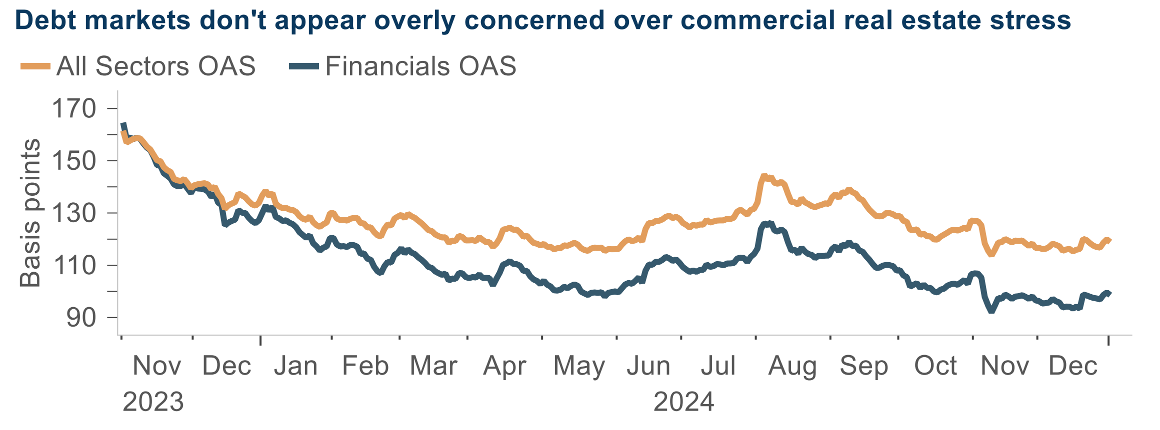
Real estate equities have the lowest correlation with a change in rates - the asset class should outperform as rates come down

Correlation: equity sector vs. change in U.S. 10-year yield



Sources: New York Life Investments Global Market Strategy, S&P Global, U.S. Department of Treasury, Macrobond, January 2025. The S&P 500 Index is an unmanaged index that is widely regarded as the standard for measuring large-cap U.S. stock market performance. Each sector is represented by the corresponding S&P 500 sector index categorized by GICS level. CS: Consumer staples, CD: Consumer Discretionary, Comm: Communications, RE: Real Estate, IN: Industrials, Fin: Financials, Mat: Materials, UT: Utilities. It is impossible to invest in an index. Past performance is not a guarantee of future results.

Debt markets don't appear overly concerned over commercial real estate stress

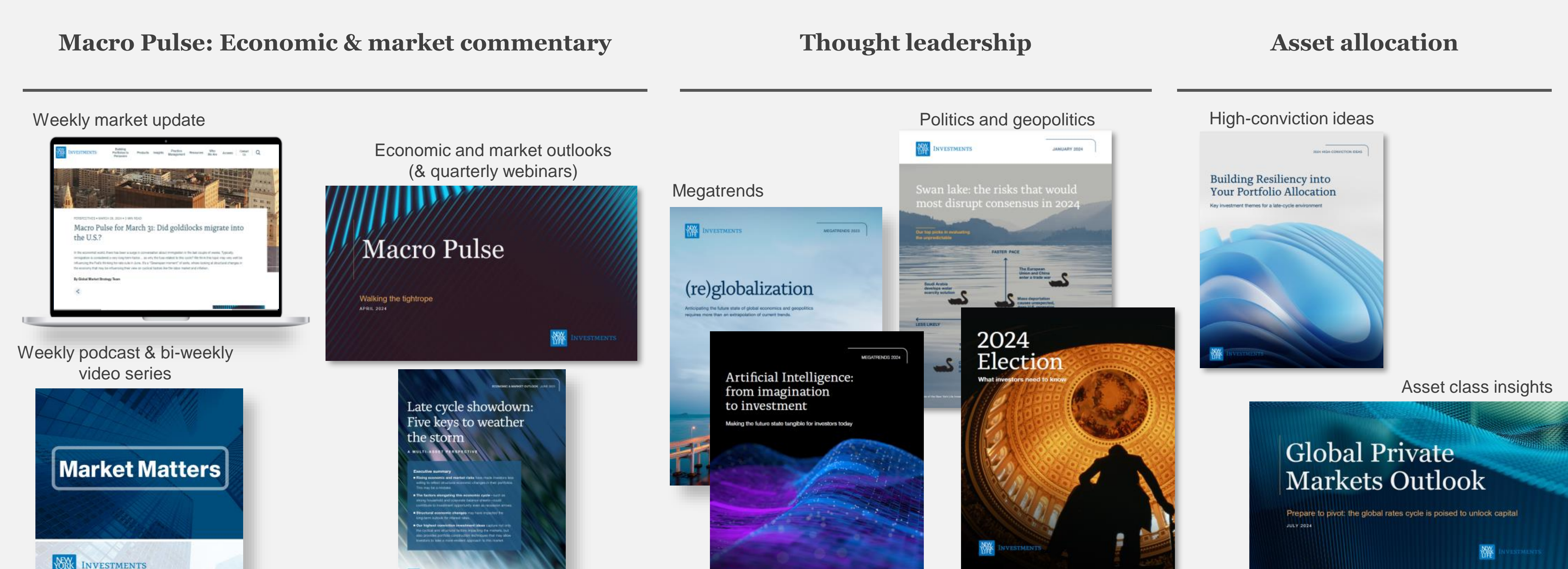


Sources: New York Life Investments Global Market Strategy, Bloomberg, Macrobond, January 2025. Investment-grade financials OAS is represented by the option adjusted spread of the Investment Grade Financials (Sr) sector. All sectors OAS is a weighted average of the option adjusted spread of the Investment Grade All Cash Bonds sector.

- U.S. commercial real estate (CRE) experienced a one-two punch in the past several years. First came the pandemic, which pushed many white-collar jobs to work at home for a time, a trend that has been sticky in the U.S. Then came the interest rate hiking cycle of 2022–2023.
- As the economy slowed, questions were raised about whether write-downs in CRE valuations could prompt a new wave of banking losses, given the outsized exposure of small and mid-cap (SMID) banks to CRE loans.
- A majority of investors, bankers, and regulators are highly focused on CRE risks. That could imply any issue bubbling up would be quickly addressed as it was in March of 2023 and may be why bank bonds are outperforming the broader market (**right chart**).
- Despite a general downturn in the asset class, liquid real estate stood out as the top performer when yields declined at the end of last year. Notably, the sector has the lowest correlation with changes in yields. We expect further cuts from the Fed could benefit the asset class (**left chart**).

TAKEAWAY: Liquid real estate could present opportunities for savvy investors. Lately, REITs haven't kept pace with the broader market, partly due to concerns about their exposure to office spaces and other less desirable assets. Yet, it's important to recognize the breadth of the REITs sector and the crucial role of active management. Wise portfolio managers have been focusing on the growing industrial and technological segments within the REITs market. We think it is worth noting liquid real estate stood out as the top performer when yields declined at the end of last year.

Global Market Strategy insights



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