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Key considerations for global equities beyond the U.S. election

From the Field
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Key Insights

- Looking beyond the election, the outlook appears relatively bright. The U.S. economy is growing, inflation is under control, and consumer and business balance sheets are in good shape.
- Supported by powerful investment trends such as artificial intelligence and GLP-1s, alongside recent economic policy measures and a broadening of market returns, 2025 has the makings of a favorable environment for stock selection.
- At the same time, fundamental changes are happening in the world that, we believe, demand an active approach to identify quality companies with improving economic returns.

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Equity markets have become more challenging as geopolitics and peaking earnings growth have contributed to increased volatility. The prospect of a new president in the White House has loomed large on investors' minds. Beyond the U.S. election, however, what might 2025 bring? The powerful investment trends of artificial intelligence and GLP-1s,[1] along with recent economic policy measures, are reasons to be more sanguine about the outlook. Our conversations with companies are adding to a sense of optimism. Meanwhile, the broadening of market returns from the concentration of the "Magnificent Seven" since the summer also makes us believe that 2025 could be a good environment for stock selection.

U.S. election remains the focus in the near term

The U.S. election continues to dominate sentiment and will until November 5. The next president of the United States is important in terms of domestic policy

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[1] GLP-1 agonists are medicines used to treat type 2 diabetes. They mimic (copy) the action of a hormone (chemical substance) called GLP-1. Your stomach naturally releases this hormone when you eat food.

but also has important implications for the rest of the world. Anxiety around the election has increased uncertainty and fed through to business and consumer confidence. A rise in risk aversion has impacted consumer behavior, with purchases being delayed and corporate projects pushed out further until after the election result. The consequence has been a more volatile market environment, with investors seeking safety in Treasuries and defensive stocks. Utilities has been the best-performing sector so far this year.

Beyond the election, however, the outlook appears brighter. The U.S. economy is growing, and U.S. gasoline prices are down 40% year over year, which has materially benefited consumers. Consumer and business balance sheets are in relatively good shape. Meanwhile, inflation has fallen to near target ranges, allowing the U.S. Federal Reserve to cut interest rates by 50 basis points in September—with indications of more to come. All this provides a relatively strong backdrop for equity markets.

Policy response at last from China

This benign view may or may not be challenged by developments in China. The Chinese economy has been exceptionally weak in recent years. It has been difficult to understand why since policymakers over the past 20 years have typically reacted to weaker conditions with stimulus measures. Chinese policy under President Xi Jinping has very much followed the CRIC-based cycle (Crisis, Response, Improvement, Complacency). We believe the Chinese economy has recently been at the Crisis stage, as evidenced by rising unemployment (especially among the young), a moribund housing sector, and a stock market out of favor with both domestic and international investors. The lack of policy response called into question the terminal values of companies in the region.

That changed in late September with a sudden and significant switch to the Response phase of the CRIC cycle. Policymakers announced a wide range of measures designed to support the economy, including specific objectives to meet annual economic targets, reverse the decline in the property market, and provide more monetary policy easing. Measures also included targeted support for the equity market and potential issuance of RMB 1 trillion–2 trillion in central government debt to support growth and individual consumption.

The measures were much needed, particularly following an extended period of inaction. Importantly, they feature a greater level of coordination of monetary and fiscal support compared with previous rounds of stimulus measures. The coordinated response and the fact that President Xi is driving the shift sends a powerful message about the intent. With valuations at record lows, asset prices have subsequently moved quite significantly in a very short period.

What are the potential implications for inflation and U.S. monetary policy?

It is important to recognize that China's weaker economy has, however, helped the U.S. Federal Reserve's recent moves to ease monetary policy. A Chinese economy operating at normal speed would have made inflation a more difficult challenge for the U.S. Federal Reserve, notably through higher prices for energy and related commodities. Instead, a weaker Chinese economy allowed the Fed to better control the slowdown, achieving what appears to be a soft landing for the U.S. economy. While unemployment has risen slightly, headline inflation is back to near its target ranges, providing the Fed enough wiggle room to adjust monetary policy. The new Chinese stimulus measures could have an impact on this, but we will have to wait and see the effects. In the meantime, China's long-term structural headwinds remain, namely the dysfunctional housing market, weak consumer confidence, and an aging population.

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Overall, we believe inflation in the U.S. is unlikely to fall below the 2% range, remaining sticky in select areas of the economy. The economy looks to be facing more of a midcycle slowdown, rather than the beginnings of a recession. Therefore, we do not anticipate a rate-cutting cycle as substantial as perhaps the markets are predicting. Further, we are not contending with a negative credit cycle as seen after the global financial crisis (GFC) or during the pandemic. Then, central banks had to slash interest rates to tackle wider structural problems. By contrast, this time around the Fed has cut rates not in response to a crisis, but more in recognition that they were simply behind the curve.

The mosaic of fundamental changes will need managing in a responsible way

The absence of a credit cycle, along with the powerful investment trends of artificial intelligence and GLP-1s, indicate a relatively benign environment. Once the uncertainty of the U.S. election is resolved, we expect looser monetary policy, Chinese stimulus, and strong consumer and corporate balance sheets to shape a favorable environment for equity markets in 2025.

That doesn't mean that everyone wins. An equilibrium shift has moved the global economy off the efficient frontier. From the GFC to the pandemic and the Russia-Ukraine war, developed economies were able to export jobs and capital to China, while China exported cheap goods in return. At the same time, the U.S. and Russia provided ample cheap natural gas to Europe's economy. These dynamics kept the global economic system very efficient and inflation levels low.

Today, we are clearly seeing a significant realignment. Entire supply chains are being rebuilt, which will take time. Countries are becoming much more strategic around their intellectual capital and energy supplies. Amid such fundamental changes, we believe active management is essential. This is where we believe our investment framework can earn its stripes. Importantly, our framework works in both low- and higher-inflation environments. We are also a great believer that the fastest learner wins, and with the game changing this will be important. As always, we continue to search for quality companies where we can identify insights on improving economic returns.

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