Allianz Global Investors

# Fundamentally Thought-provoking

## Quarterly perspectives from Dr Hartwig Kos

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**Never mind MAGA, equities are already great *again!***

Another month, another reversal! While the world is recovering from "Trump's Trade Tornado", equity markets are once more in full swing. Since April's "peak angst" the S&P has staged a swift 20%+ reversal in a mere 36 days. A record move only topped by more ferocious recoveries in 2009 and 2020. The most staggering aspect about all this is the fact that global equity markets are again close to all time highs. The German equity index, the DAX, has hit this important psychological level already a few weeks back, and the S&P is just a few hundred points off it.

Yet, institutional investors across the globe are as bearish as ever and are hurting because they missed most of the recovery so far. Flow statistics suggest that retail investors "bought the dip", helping carry the rally so far. Well, who can blame retail punters if US President Donald Trump tweets "THIS IS A GREAT TIME TO BUY!!!" more than once in the last month!

So, what is next? (...isn't it obvious? )

Most of the uber-bearish Institutions are probably going to get "squeezed in" and markets might well continue to go up further. It is tempting to say that the sky is the limit, but that is not realistic. A more level-headed projection is to assume that Global equities have another 15%+ in them before the end of the year. We would also not be surprised to see the S&P hitting the magic 7k sooner rather than later.

We always emphasise that no one has a crystal ball, but everyone has their views. In our fundamental assessment, the risk to equity markets is to the upside, and investors, particularly institutional ones, are not fully discounting that yet. Furthermore, we would also be unsurprised if global equity markets see strong returns in the next few months.

While there is a clear secular shift out of the US in favour of international equities, a powerful equity bull run could challenge this trend for a while.

## Multi Asset observations: our highlights

**Stractical perspective** – Risk in equity markets is skewed to the upside. Over the coming months investors are at risk of getting squeezed into a potentially quite powerful equity market rally. Buy equities into strength or if the opportunity arises, buy into a dip. The key is to further phase into equities. Aim for heavy allocations to risk assets north of 70%. The picture for duration is somewhat ambiguous at this point, but one should not be surprised if global, and particularly US government bond yields, were to trend lower from here. As for foreign exchange dynamics, the US dollar is at risk of trending lower.

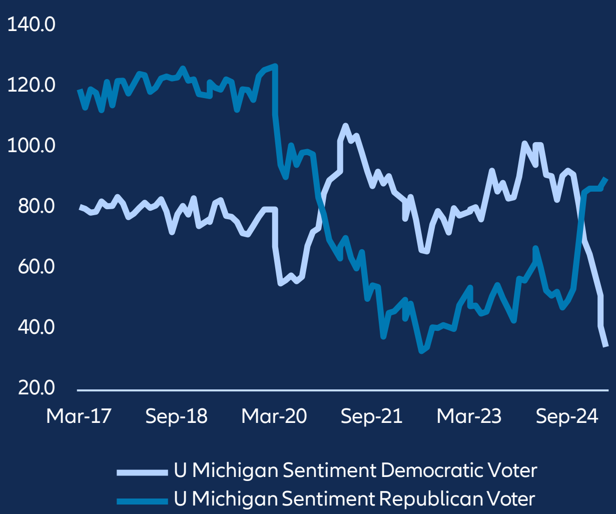
**US tech stocks vs. rest of the world** – We recognise that a scenario where US assets approach a secular top is becoming increasingly likely. High price-to-earnings valuations, paired with stark levels of index concentration, high government indebtedness, and a massively isolationist and spend-thrifty political regime do not bode well for US equities or bonds. But we are not there yet. In our view, overseas investors have started to allocate away from US assets prematurely as the risks of a strong catch-up rally are underestimated.

**Emerging market hard currency bonds** – This idea also follows the logic of investors pivoting away from US assets, but it has also to do with the US administration's focus on weakening the dollar. It is evident that FX considerations are an important part of the US's trade negotiations (for instance, with South Korea and Japan). While local currency emerging market bonds should do much better in a soft dollar scenario, the comparatively lower risk nature of hard currency bonds makes the asset class appealing to us at this point.

## Perception is reality…

…goes the saying of Lee Atwater, a political strategist who served in the Ronald Reagan and George HW Bush administrations, expressing, “that whatever someone sees or feels to be valid (regardless of whether it is or not) is their truth.” There is lot of merit in this observation, particularly in a populist world.

**University of Michigan survey of consumer sentiment by political affiliation**




Source: University of Michigan April 2025

Hence it should come as no surprise that sentiment amongst US consumers depends on whether one votes blue or red (shown in the chart above). Still, regardless of rose-tinted glasses, it remains a fact that the ongoing uncertainty about global trade has taken its toll on confidence, so the weakness in soft data is not unexpected. Moreover, many US companies front-loaded international orders in anticipation of punitive tariffs. Hence, it is only a matter of time until hard activity data catches up with sentiment and turns weaker too. In short, the US economy might have already fallen off a cliff, and the data will eventually reflect this new economic reality. The expectation is that the Federal Reserve (Fed) will not be able to ride to the rescue swiftly given all the prevailing uncertainties that pose upside risks to inflation. The broad assumption is that markets have run too far and will likely face another substantial setback. With further weakness in US equities imminent, the belief is that there will be an ongoing reallocation out of the US to the rest of the world.

*But let us play devil’s advocate and entertain an utterly non consensus scenario for a moment, what if…*

**a) Mr Trump’s trade war has already peaked?**
What if the trade war narrative has more to do with foreign exchange markets than anything else? In the talks with Japan and South Korea, FX considerations are explicitly mentioned, so what if “Liberation Day” was indeed the “Mar-a-Lago Accord” and in 12 month's time there are no tariffs whatsoever, but the dollar is 20% lower? Yes, that sounds bonkers, but Trump tends to change his mind rather frequently, remember “DOGE” that didn’t last long either. Keep in mind, a nasty long drawn trade war will not help him with the midterm elections.

**b) There is no US recession?**
US imports took a recent nosedive, falling 20%. But the Atlanta Fed GDP tracker just signalled a significant upswing in projected US activity from 2.2% to 4.6% growth, which exceeds even the most bullish forecasts about economic growth by more than 1%. Granted, the Atlanta Fed measure has become rather volatile in recent months, but what if the imports brought forward in anticipation of tariffs, have already dented economic growth? What if a swift end to the trade war, ie, TACO (Trump always chickens out) allows sentiment indicators to recover again, and investors become inclined to look through the softening hard data? What if the “big, beautiful” tax bill cuts and further deregulation help avoid the economic cliff that everyone fears?

**c) The Fed blinks?**
From an almost failed US Treasury auction to US mortgage rates at close to 7%, soaring credit card and car loan delinquencies, sluggish initial public offering activity, a looming corporate refinancing wall, and an emerging housing crisis in Florida, there is a lot of scope for the Fed to blink.

**d) Institutional investors wear rose-tinted glasses too?**
What if institutional investors are alienated by unpredictable US policy and subconsciously expect the Trump administration to fail? If so, they would turn cautious on equity markets (as many seem to be now). Given the swiftness of the recent recovery, it is only a matter of time before institutional bears change their stance, watch out …Melt-up?! (well, who knows).

*To be clear, we think that US assets and, in particular, equities are set for a secular top, while other regions have the potential to outperform. The key question is sequencing, and we are conscious that the S&P 500 and the Mag 7 may have one last catch-up rally!*

**Disclosures**

The MSCI All Country World Index is a free-float weighted equity index, and includes both emerging and developed world markets. The FTSE World Government Bond Index- Developed Markets measures the performance of fixed-rate, local currency, investment-grade sovereign bonds issued in developed markets. The Bloomberg Dollar Spot Index tracks the performance of a basket of ten leading global currencies versus the U.S. Dollar. Each currency in the basket and their weight is determined annually based on their share of international trade and FX liquidity. The S&P 500® index includes 500 leading companies and captures approximately 80% coverage of available market capitalization. The MSCI EMU (European Economic and Monetary Union) Index is a free-float weighted equity index. The TOPIX, also known as the Tokyo Stock Price Index, is a capitalization-weighted index of all companies listed on the First Section of the Tokyo Stock Exchange. The MSCI EM (Emerging Markets) Index is a free-float weighted equity index that captures large and mid cap representation across Emerging Markets (EM) countries. J.P. Morgan's developed and emerging market indices track fixed rate issuances from countries spanning the globe. The Bloomberg Barclays US Corporate High Yield Bond Index measures the USD-denominated, high yield, fixed-rate corporate bond market. S&P GSCI Crude Oil Total Return index is weighted based on world production and it uses Spot Prices to calculate the price. Bloomberg Commodity Index (BCOM) is calculated on an excess return basis and reflects commodity futures price movements. The Bloomberg Barclays U.S. Aggregate Bond Index represents securities that are SEC-registered, taxable, and dollar denominated. The index is composed of securities from the Bloomberg Barclays Capital Government/ Credit Bond Index, Mortgage-Backed Securities Index, and Asset-Backed Securities Index. It is generally considered to be representative of the domestic, investment-grade, fixed-rate, taxable bond market. Unless otherwise noted, index returns reflect the reinvestment of income dividends and capital gains, if any, but do not reflect fees, brokerage commissions or other expenses of investing. It is not possible to invest directly in an index.

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