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iFlow

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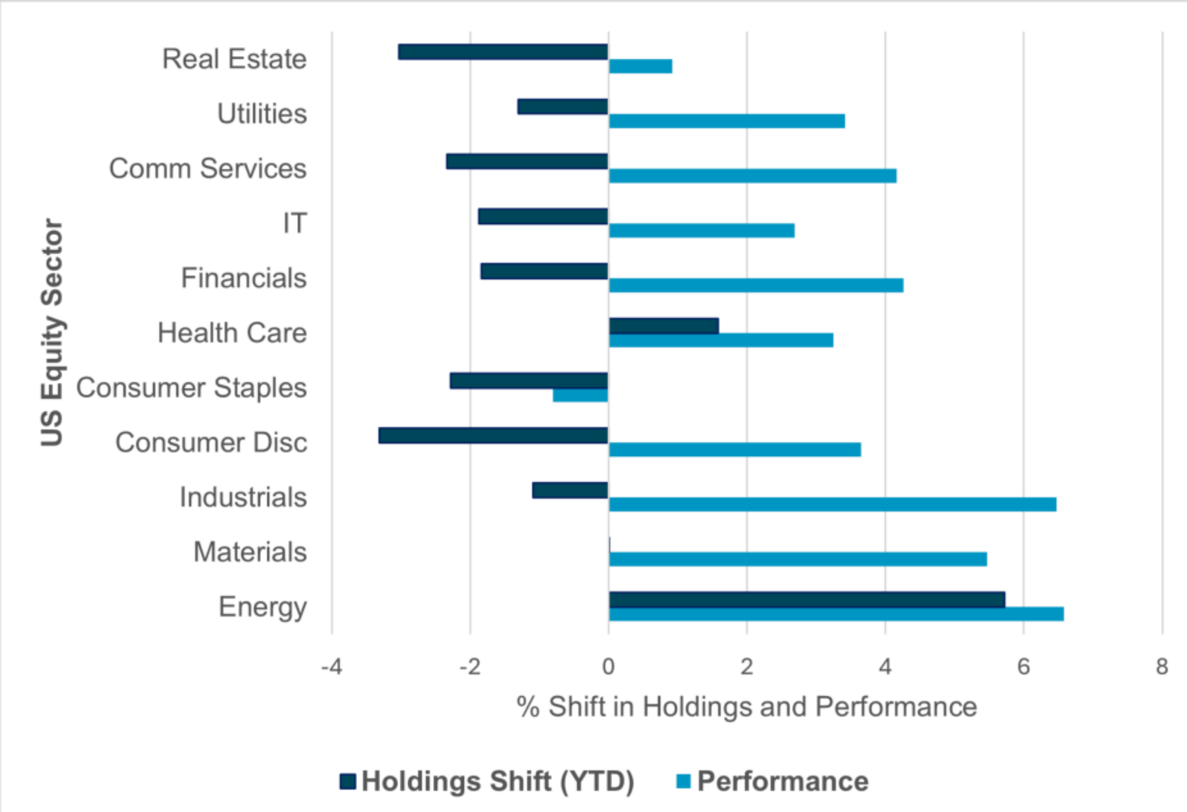
US Equity Allocation and Trump 2.0

- The first four days of President Trump's second term have led to significant uncertainty in FX markets, with clear shifts in global flows of equities and fixed income, and notable changes in holdings of US equity sectors, led by Energy, Materials and AI/Tech.
- Surprisingly, this week volatility and the USD are lower, while global stocks are higher, led by Europe, including Germany's DAX and Sweden's OMX, while Chinese and Hong Kong exchanges are down.
- We can see structural and cyclical forces at play for the weeks ahead. The set-up for some sectors in the US is for more trouble – with our equity shorts in Real Estate higher, while IT and Communications are lower showing the current mood into critical Q4 2024 earnings.

Trump's executive orders, speeches and press appearances have had a significant impact on how investors believe the new administration's policies will affect markets going forward. The new president made history by signing 26 executive orders on his first day in office, far exceeding the nine signed by Biden and two by Obama on their first days as president. Over the course of his first term Trump signed a total of 220 executive orders, while Biden signed 162 in his term and Bill Clinton signed 200 in the first of his two terms. The topics not included in the orders stand out: tariffs and crypto. The initial market reaction has been relief, particularly around trade policy, as investors view the discussion of tariffs as more of a negotiation tool than a method for rebalancing US trade deficits and adding to US federal revenue. Whether this proves to be the case remains an open question, with February 1 set as the new deadline. Of the orders that matter most to markets the one related to energy was the surprise. We can see this most clearly from iFlow data, which show increased holdings matching the performance of the market year to date.

Exhibit #1: iFlow US Sector Holdings vs. Performance



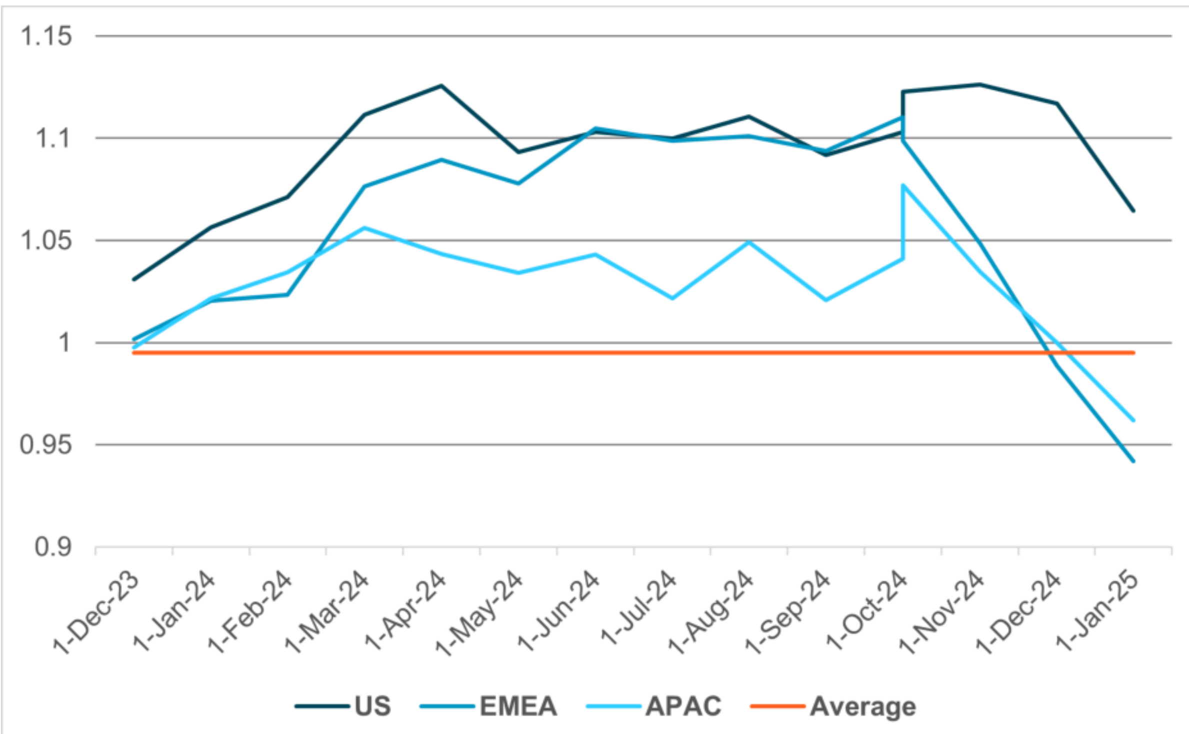
Source: iFlow, BNY

Supply traditionally means lower, not higher prices. The oil markets touched 2-week lows on Wednesday, but year to date WTI crude oil futures are up 5.5%, holding at well over $75 bbl. The role of better global demand hopes from Europe and Asia are part of the story, along with weather and the war between Russia and Ukraine. As the Wall Street Journal noted, the president "directed agencies to support the development and transportation of fossil fuels, the build-out of electricity transmission infrastructure, and the advancement of uranium production and geothermal energy." In his address to Davos, Trump called on OPEC to help lower oil prices.

Asset allocation pressures from January are a notable consideration for investors. The first year of a new president has over the last 100 years seen a mostly positive outcome 58% of the time. However, this time, value concerns dominate the landscape with investors clearly cutting back after two years of outsized returns. The regional comparisons still favor US outflows and EU and APAC inflows. The risk for

US investors is in the CAPE comparisons between regional bourses and the current holdings lacking diversity. The current US Shiller PE is 38.37 while the EuroStoxx 600 is 26.38 and the Asia markets are 23, with the most undervalued bourse being Singapore. The notable shift in holdings from fourth quarter across the world reflects the usual behavior we see after outsized gains in equities, as we did throughout 2024. What stands out is that this has continued into January. Our data show US equity holdings remain 5% over the 5Y average while APAC is 2% and EMEA 4% below average.

Exhibit #2: How Risky Are APAC and EMEA Shares?

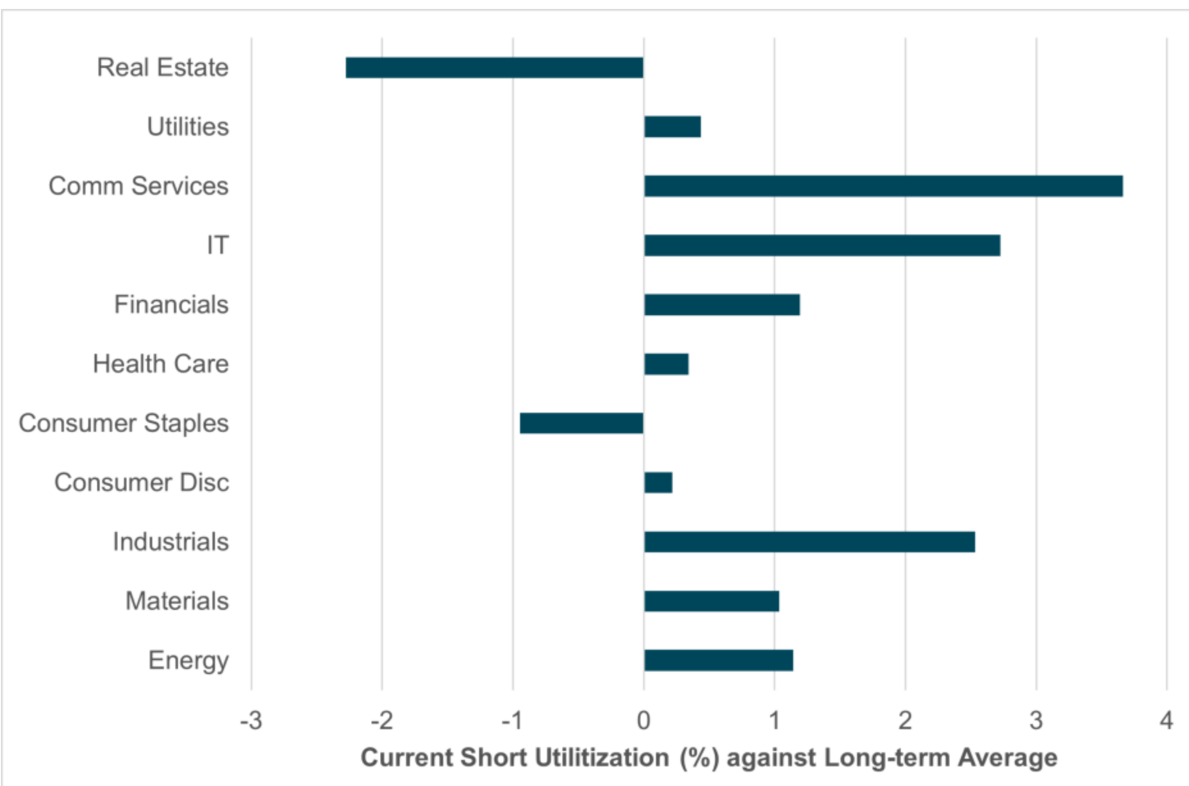


Source: iFlow, BNY

The narratives of 2024 remain important to investors in 2025 – this became clear with Trump’s announcement of cross-border investments into the US with his Stargate project, a plan for up to $500bn in investments in AI projects, data centers and chips over the next four years. The project also lifted hopes for health care, given Oracle’s role in the project and the push for new cancer treatments. The blurring of sectors and companies in the S&P 500 has broader implications for portfolios given the concentration of companies in the S&P 500 index. As we can see from the short flows and utilization data, IT and Communications short positions are well below long-term historical averages. The type of investors that use short positions are a subset of the larger real money flows shown in our holdings. The velocity of position shifts and their bias to vary from a benchmark are different, making the holdings and shorts view of our data more powerful in painting a bigger picture for investor risk analysis. Clearly the focus on Real Estate and the cyclical Consumer Staples sectors reflects some concern about rates, inflation, and the clash between Trump's policies and the FOMC's moves. On the other hand, there is faith in IT, Communications and the rebirth of US industrial investments.

Bottom Line: The focus of the weeks ahead will continue to be in the dynamic tensions between normal cyclical economic forces driving FOMC easing hopes and labor markets against the plans by the new US administration to change trade, fiscal and regulatory policies to lift US growth. The AI, Energy and Industrials sectors have led in the first few weeks of 2025. This will now be tested by the bottom-up analysis of Q4 earnings and Q1 outlooks for the big names in those sectors – including Nvidia, Amazon and Alphabet. All three companies are expected to report earnings in the weeks ahead. As for Health Care, the focus will be on Eli Lilly and Merck, whose earnings are expected to be among the top 10 for the quarter. The Energy sector is the one area where surprises are most likely as analysts see double digit drops in earnings approaching −30% y/y. The subsectors to watch are Storage and Equipment as new policy shifts to drill are expected to find some early Q4 support.

Exhibit #3: iFlow US Equity Short Utilization vs. Long-term Average



Source: iFlow, BNY

Please direct questions or comments to: iFlow@bny.com

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