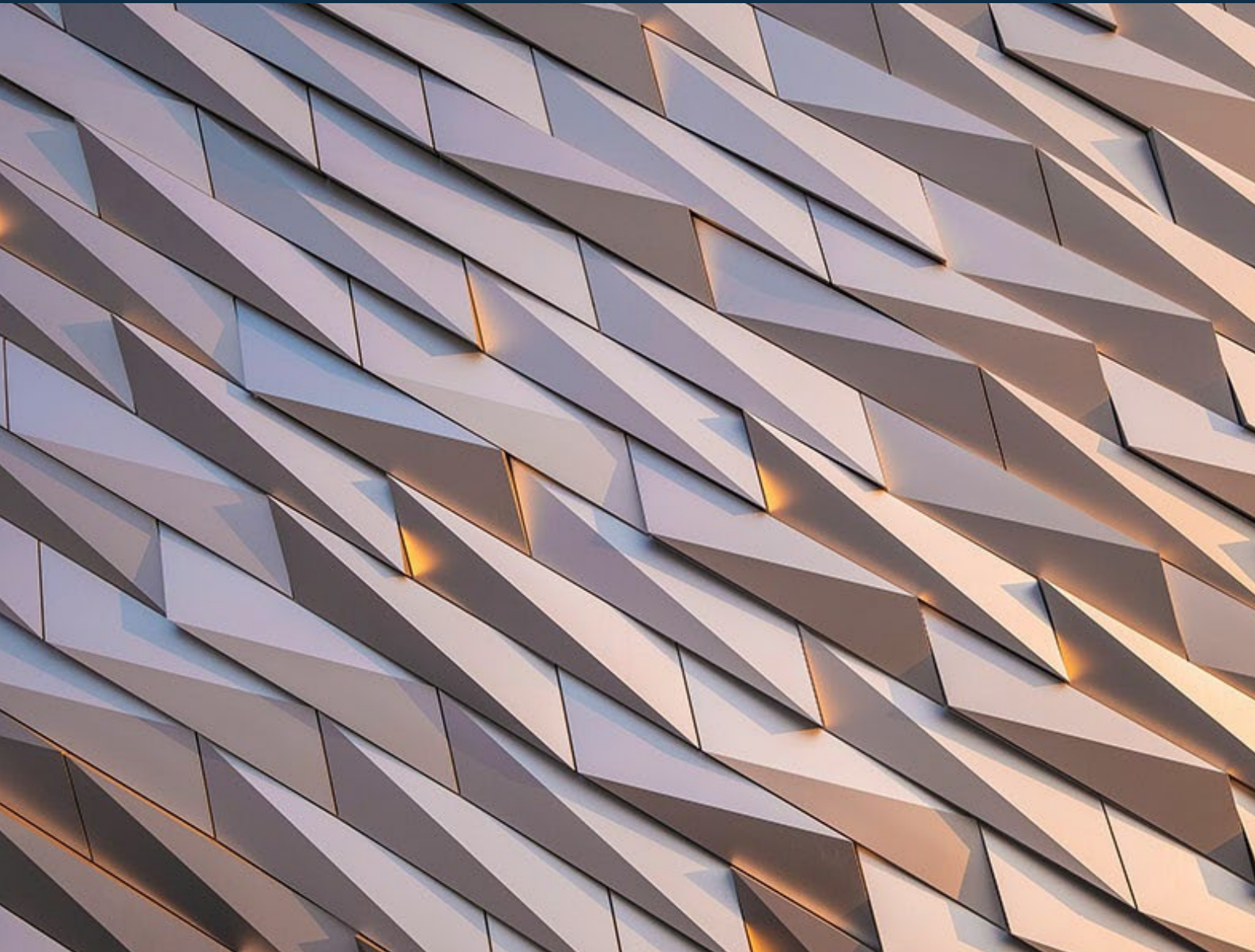


EVLI

# Atlas Monthly Equity Navigator

MAY 2025



## After April Storms, May Sunshine Emerges (With Caveats)

The "Trump-retreat" narrative, where aggressive trade stances soften, gained further traction in May. Preliminary talks with China saw a significant reduction in threatened US import tariffs, reportedly from a headline 145% down to 30% on certain goods, followed by a welcome pause in tariff rhetoric towards the EU. This provided further relief to markets still jittery from April's volatility.

Elsewhere, the spectre of ever-rising national debt levels continued to unsettle bond markets, particularly in the US and Japan. The US fiscal plan, signalling increased spending and a persistently high deficit, contributed to a quarter-percent rise in 30-year bond yields in both countries over the month. In Europe, fiscal expansion led by Germany remains on the horizon, with the new German government indicating ambitious plans. However, the crucial question lingers: when, and if, will economic fundamentals align with these heightened expectations?

For relative returns and valuations to hold, a catch-up in corporate sector fundamentals, especially earnings growth, is essential. European Q1 earnings were still in negative territory, yet significant dispersions between sectors underscore that a regional European equity allocation continues to work best through a thematic lens, such as Defence or German-focused stocks. The AI theme, far from being extinguished, was reaffirmed by robust reports from hyperscalers and Nvidia. Nonetheless, US trade policies and the simmering technological 'cold war' between the US and China pose major risks for US tech giants. The potential for unexpected "DeepSeek"-style revelations, like those experienced in February, also looms. Despite these headwinds, AI demand remains healthy as companies actively leverage it to cut costs, boost productivity, and spur new growth.

### 1. Recession Risks Fall, but Slowdown Looms

- **Odds for a US recession halves:** The Polymarket odds for recession in 2025 notably dropped from 65% at April's end to 33% by the end of May. This shift was largely attributed to President Trump's retreat from the most aggressive tariff policies, prompting economists to lower recession probabilities.
- **Global slowdown is still on the cards:** Effective tariffs will remain significantly higher than at the start of the year, and most soft macroeconomic indicators continue to point towards uncertain times ahead.

### 2. Companies Cautious – Capex Chills Amidst Lingering Uncertainty

- **Capex slowdown likely:** The most obvious hit from the still-high uncertainty will likely be a slowdown in corporate sector capital expenditures (capex). However, capex nowcast data have not indicated any weakness yet.
- **Size matters:** The magnitude of this slowdown is still unclear, as most companies have not signalled significant damage yet. What damage this economic uncertainty and potential price shocks might ultimately have on employment and consumption remains to be seen.

### 3. Markets in Wait-and-See Mode – What Next After the Rebound?

- **From panic to relief:** Following the panic in early April and the subsequent impressive rebound in equity markets through late April and early May, equities have largely moved sideways in recent weeks.
- **Waiting for the next catalyst:** Typically, markets look for some type of trigger after a big rally, which could further boost or break the rebound. The most obvious signals may come from macro data and bond markets, especially as tariff noise continues to wane. It's possible that economic data may stay resilient in the early summer, while Q2 earnings growth may not be as bad as initially feared.
- **Signs of a slowdown:** The economic slowdown has probably already started, evidenced by weakening PMI and ISM business surveys, but late summer will likely be the period when we could start seeing the stagflationary drags of weaker growth and rising inflation.

## Global Equity Performance

- After a negative April, global equities rebounded in May, marking their first advance since January with a gain of 5.8%. Cyclical sectors and US stocks (6.3%) led this recovery. Other major markets, including Europe (5.1%), Japan (5.0%), and emerging markets (4.4%), also posted positive returns but trailed the US.

- Germany (6.7%) continued its notable outperformance, extending its year-to-date gains to over 20%.

## United States

- Following a weak April, US markets experienced a strong relief rally. This was driven by cyclical sectors (8.8%) and mega-cap technology stocks (notably the "Magnificent 7," which gained 11.9%), supported by a robust earnings season.

## Europe

- In Europe, the aerospace & defence sector (15%) saw exceptional performance as the defence investment theme gathered further momentum (see details below).
- Among broader cyclical sectors, technology (7.8%) and industrials (7.5%) also delivered strong returns in May.

## Emerging Markets

- Emerging markets (4.4% overall) lagged their developed market counterparts in May. Notably, Brazil (1%) and India (1.2%) underperformed. China (2.8%) posted a modest gain but also trailed the performance of larger Western markets.

## Themes & Styles

- **European Investment Themes: Navigating Trade Tensions and Rising Defence**

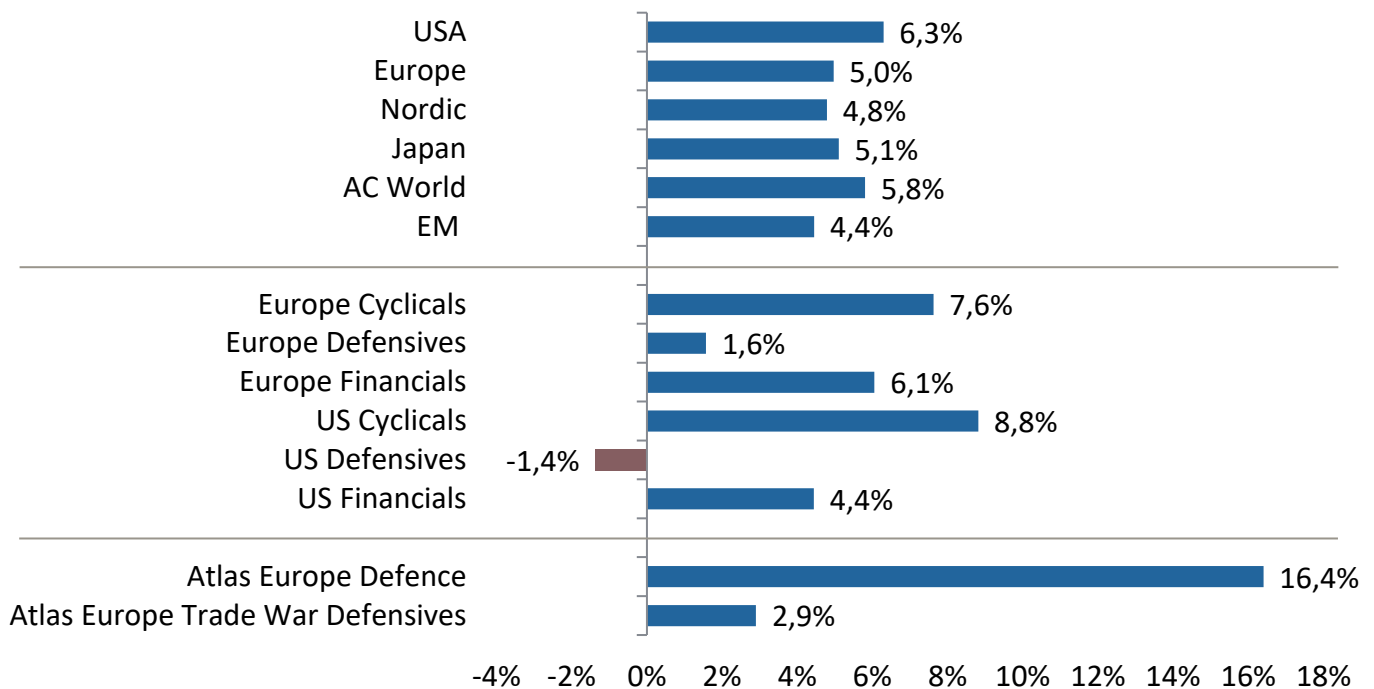
Trade War Defensives: Europe faces potential US tariffs, casting a shadow on its exporters. However, unlike potential US fiscal tightening, Germany and other European nations are pursuing fiscal stimulus. In a trade-war-induced slowdown, a defensive strategy involves focusing on Europe (due to its stimulus) and selecting non-cyclical, 'quality', and reasonably priced 'value' companies resilient to tariffs and slower growth.

Europe Defence: Separately, European defence spending is poised for significant, double-digit growth, driven by heightened geopolitical tensions and expected to be less sensitive to economic weakness than in past cycles. This theme gains a defensive character from rising budgets and a potential allocation shift towards domestic European firms. Investing in 'pure-play' defence companies, screened for quality and growth while managing diversification, aims to identify long-term sector winners, though a prolonged recession could temper spending plans.

- **Artificial Intelligence: Alive & Kicking, Global Competition, and Capex Considerations**

The AI sector is entering a dynamic new phase, as the emergence of competitive models like DeepSeek from China signals that AI growth is not confined to a few U.S. tech giants, suggesting an evolving investment theme. AI agents are achieving significant breakthroughs, poised to substantially boost worker productivity, particularly for early-adopting firms, with software companies like CRM providers set to be prime beneficiaries of these enhancements. Indeed, Goldman Sachs projects AI could expand net margins for U.S. large-cap companies by a notable 4 percentage points over the next decade. While the U.S. currently hosts most AI firms, China is rapidly closing the gap, indicating a broadening global AI ecosystem, and lower barriers to entry in some segments may spur further investment from new market entrants, intensifying competition. However, AI-related capital expenditure (capex) remains elevated. While necessary for capacity building in an innovation cycle, this could become an headwind, as historically, capex-heavy firms usually underperform in the long term. For investors, this means the AI landscape offers compelling growth driven by productivity gains and broadening global participation, but these opportunities must be carefully weighed against the potential risks associated with high capital expenditure and the historical performance trends of capex-intensive sectors.

## Atlas Equity Chart of the Month: Equity market returns, euro returns in May 2025



Source: Evli Atlas Portfolio Technologies; Total returns in euros.

### Navigating Choppy Waters as Slowdown Looms

Tariff risks appear to be waning, partly due to a tendency for escalations to be tempered when markets or the economy show weakness. However, episodes of tariff escalation might still occur over the summer. Simultaneously, the global economy is expected to enter a period of slower growth in the second half of 2025. For example, Morgan Stanley forecasts global GDP growth to be a full percentage point lower, at 2.5% at the end of 2025 (Q4/Q4) compared to 3.5% at the end of 2024. They also project US GDP growth at 1.0% (Q4/Q4 2025), down from 2.5% at the end of 2024. Other forecasters anticipate a similar path for the global economy, attributing the slowdown to higher tariffs, rising inflation, and persistent high levels of uncertainty.

We continue to advise cautiousness, though somewhat less so than after April, amid lower risks of a global earnings recession. It's always worth remembering that earnings growth drives equity returns. However, slower capex growth presents a risk for earnings growth, as these tend to correlate. Furthermore, corporate margins are at risk amid potential rising tariffs. Hence, the stance remains to maintain exposure to tariff-resilient defensive firms, as well as defence stocks in Europe and AI-related themes from a global perspective.

### What is Atlas?

Atlas is an intelligent platform empowering investors to build and manage highly personalized equity portfolios. Leveraging data and AI, we craft strategies aligned with your precise investment style, objectives, and sustainability goals—from classic value to emerging themes like AI.

- **True Personalization:** Go beyond generic models. Our AI helps craft strategies that perfectly reflect your vision.
- **Unprecedented Flexibility:** Don't get locked in. Shift from value to growth, or adjust thematic tilts, as your outlook evolves.
- **Powered Customization:** If our expert-designed, ready-made portfolios don't fit, our Atlas team of seasoned portfolio managers with the help of our proprietary AI engine will build a unique strategy for you.

**Invest intelligently. Adapt instantly. That's Atlas.**

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