November 2024

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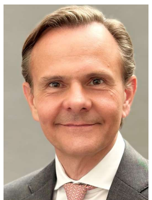
Market outlook

#1 Market & Macro

US election likely to lead to a change of favorites in equities


Björn Jesch

October proved to be a poor month for investors, on stock and bond markets alike. The S&P 500, usually breaking record after record, experienced the first negative month in six months, and 10-year US Treasuries lost four percent on the bond market.
"Public debt has obviously made inroads in the minds of investors", Björn Jesch, global DWS Chief Investment Officer, states. This has become obvious in both, the United States, where concerns of ever increasing public debt have markedly pushed up rates for long maturities, and in the United Kingdom. In face of an expected rate-cutting cycle by central banks, Jesch remains strategically constructive on corporate bonds.
"However, we have downgraded our long-term favorites – investment-grade European corporate bonds – tactically, i.e. short-term, to 'neutral' since there is hardly any scope for a tightening of spreads to sovereign bonds."

With a view to stocks, Jesch expects changes after Donald Trump winning the US presidential election to be of minor importance for the overall market than for individual sectors. "However, if 10-year Treasury yields start moving towards five percent, this could create strong headwinds for stocks," Jesch adds. Investors now must decide whether they prioritize the fear of higher inflation and thus fewer interest rate cuts by the Fed or the expected more business-friendly policies of Donald Trump.
A further reduction of corporate taxes could boost S&P500 profits by 3 to 4 percent, however not before 2026, Jesch cautions. Corporations with a high share of domestic, i.e. US profits, would benefit most. These are mainly in the financial sector or in the market segment of small- to mid-caps.
Markets outside the United States are, however, at least for the time being, facing rough times due to the unpredictability of the incoming President, the DWS chief investment officer expects.

Topics driving capital markets

Economy: decent growth in the United States, Spain particularly strong in the Eurozone

- Consumption continues to drive the US economy. The annualized growth rate for the third quarter is 2.8 percent after 3.0 percent in the second quarter.
- Growth rates from the Eurozone surprised slightly on the upside: the third quarter registered a plus of 0.4 percent (Q2: 0.2 percent). With a growth of 0.8 percent, the Spanish economy proved to be particularly strong, boosted by continuing tailwinds from tourism.

Inflation: prices have slightly risen again

- Eurozone inflation has risen to 2.0 percent in October (September: 1.7 percent). Core inflation – excluding food and energy – stayed at 2.7 percent.
- In Germany, the inflation rate rose to 2.0 percent in October (after 1.6 percent in September), driven by higher food and energy prices.

Central banks: further rate cuts expected

- In mid-October, the European Central Bank cut its key rates by 0.25 percent to 3.25 percent. We expect another rate cut in December.
- The Federal Reserve should continue to closely watch inflation. Its further rate path will depend on incoming data.

Risks: high stock-market valuations and geopolitical crises

- High valuations on stock markets might prove a factor substantially limiting further price potential – particularly since growth of corporate profits is slowing down towards historic averages.
- Apart from Russia's war of aggression against Ukraine, the unstable situation in the Middle East is another spot of geopolitical concern, particularly the further escalating conflict between Iran and Israel.

Forecasts are based on assumptions, estimates, views and hypothetical models or analyses which may prove to be incorrect.
Source: DWS Investment GmbH, as of 06 November 2024

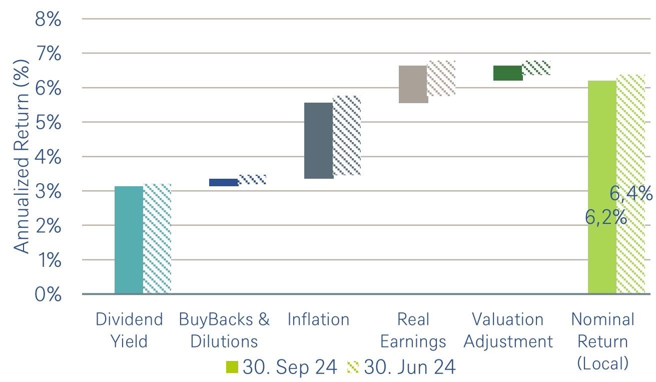
Dividends could regain more importance for stock performance

Growth or value stocks – the question of favorites seems to be a rather rhetorical question. The past ten years have only recorded two years – 2016 and 2022 –, in which value stocks have taken the lead," Thomas Schüßler, Co-Head Global Equities, states. The currently very high valuations, particularly of tech stocks, are far from being a reason of blocking a further upward path of these papers. Following the trend is the order of the day.
This does, however, not mean that there are no good reasons for investing in value stocks, for example via a dividend strategy. Investors also appreciate good risk management since there will always be setbacks. Not every investor strives for maximum returns at maximum risk," Schüßler argues. Particularly promising are dividend papers from the financial sector, utilities or oil corporations, which tend to have very high dividend ratios. Picking interesting dividend stocks on the US market is currently difficult. S&P 500 dividend returns of 1.2 percent are substantially underperforming the average of the past twenty years of 2.0 percent. Even if high valuations are not regarded as an indicator of an imminent slump, it can be assumed that shareholder returns of the next few years might fall short of their long-term average.
"Looking through the windscreen, I rather see returns of five percent and not the eight or ten percent achieved in the past," Schüßler comments. Current valuations could be seen as premature returns. They are far ahead of the current profits of corporations. This is another argument in favor of dividend stocks, the performance of which is based on both, dividends and price gains. With a view to the US market, the most important stock market of the world, Schüßler regards high public debt as a risk.

Currently, public debt is still having a positive effect on the stock market. But high public debt in combination with a falling saving rate and rising debt of private households is a problematic constellation. "High private debt currently supports the stock market. People continue on their shopping sprees without forcing corporations to substantially increase wages," Schüßler argues. But at some point, a threshold will be breached. This might result in rising bond yields, probably putting stock markets under pressure.
Against the background of this rather risky situation on stock markets and the increased danger of setbacks, Schüßler is, apart from dividend stocks, also warming to gold and gold mining equities. "Diversification and capital protection are their major positive aspects," Schüßler concludes.

Dividend yields: an important part of total returns

Expected composition of stock returns



Source: DWS Investment GmbH, as of end of October 2024.

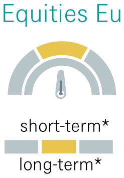
Equities USA: stronger focus on domestic corporations

- Tech stocks, led by stocks around the topic of Artificial Intelligence, are the main drivers for the US stock market to remain the market with the by far highest valuations.
- Since president-elect Donald Trump is expected to focus on profits made within the United States and to cut corporate taxes, tech stocks operating in a global context should benefit to a lesser degree than domestically oriented corporations.

Equities Germany: prices higher than warranted by fundamental data

- It runs and runs and runs – this seems to be the motto of the German leading Dax index – and this although data are not extremely convincing. The current reporting season was rather mixed. Profit expectations for 2025 were revised downwards, contrary to the rest of Europe.
- Against the background of this good price performance despite mixed corporate data, we are rather cautious on German stocks.

Equities Europe: implications of US election somewhat weaken the outlook



- The performance of European stocks, which are still trading at a record spread to US stocks, clearly shows that extraordinarily low valuations do not automatically culminate in prices catching up.
- Before the results of the US election, Europe was our most favored region. However, the imminent imposition of tariffs on a significant scale could dampen the outlook for European corporations.

Emerging Markets: no turnaround of the Chinese stock market on the horizon yet

- We are neutral on Emerging Market stock markets as a whole. The focus continues to be set on China and probably positive implications of further expected state stimulus programs on the markets.
- With a view to the performance of the Chinese stock market, we rather err on the side of caution, expecting the market to hover around its long-term average valuation level.

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#3 Multi Asset / Fixed Income

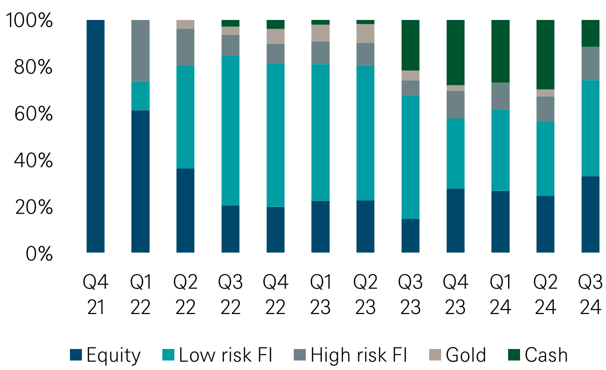
Short-term market setbacks offer opportunities in risky assets


Henning Potstada

How will the numerous economic and geopolitical uncertainties impact the weighting of asset classes in a portfolio? “With a view to risk preferences, we remain neutrally positioned in our allocation portfolios,” Henning Potstada, Global Head Multi-Asset, states. Potstada expects a further steepening of the yield curve so that the yield spread between long and short maturities will widen. “Moreover, in a market environment, in which growth concerns have replaced inflation concerns, duration should be able to contribute to portfolio stability,” Potstada explains.
All in all, allocation portfolios will remain neutrally positioned with a view to fixed income although yield levels are all but unattractive compared with stocks. As to stocks, Potstada observes two opposing developments: “Our base scenario with rate cuts combined with the avoidance of a recession would warrant a positive assessment of stock markets. But a further rally on stock markets could be contained by ambitious valuation levels – particularly in the United States – and a continuing weaker macroeconomic picture.” Generally, short-term market setbacks will offer entry points into high-risk assets.

Bonds remain important yield earners

Sample allocation for a target return of four percent



Source: DWS Investment GmbH, as of end of September 2024.

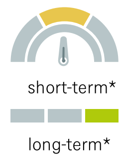
US government bonds (10 years)

Yields set to rise again

- The election result has increased the risk of higher inflation rates in the United States.
- We expect higher yields for all maturities.

German government bonds (10 years)

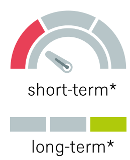
Yields should have peaked



- 10-year Bund yields have started to climb strongly again of late.
- Over a 12-month horizon, we expect a slight decline.

Emerging Market sovereign bonds

Tighter yield spreads – hardly attractive in the short run

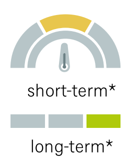


- Yield spreads of sovereign bonds from Emerging Markets have substantially tightened.
- For this reason, we have downgraded these bonds short-term.

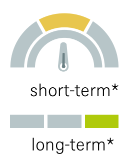
Credit

Investment Grade

USA

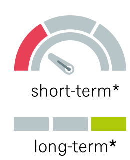


Eurozone

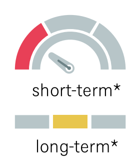


High Yield

USA



Eurozone



#4 Currencies

Euro/Dollar: **Much uncertainty around the dollar, short-term rather somewhat stronger**

- The exchange rate of the dollar will be decisively impacted by the potential imposition of punitive tariffs, further trade sanctions and the amount of future increases of public debt in the United States.
- Since US economic data are beating expectations, the dollar should rather appreciate short-term.

#5 Alternative assets

Gold: **handsome price gains in the year to-date – outlook should remain positive in the face of numerous uncertainties**

- October has been the fourth month in a row witnessing rising gold prices, meanwhile reaching a new record high of 2,790 dollars. Year-on-year, the precious metal registers gains of 27 percent.
- The demand of gold should remain high, supporting its price development even if the election risk premium might contract slightly.

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Glossary

Basis points
One basis point is equivalent to 1/100 of a percentage point, one hundred basis points are equivalent to one percentage point.

Dax
Market capitalization-weighted index, with the 40 most important listed companies in Germany. Performance index, which includes dividend payments.

Duration
Interest rate lock-in period of fixed-interest securities, which is specified in years. Helps to calculate the interest rate risk.

Growth Stocks
Shares of companies that record above-average growth rates in sales and profits compared to other public companies.

High Yield (HY)
Corporate bonds from issuers with a poor credit rating – these papers generally offer comparatively high interest rates.

Investment Grade (IG)
Corporate bonds that are deemed by rating agencies to have a low risk of default (at least medium credit rating).

Price-to-earnings (P/E) ratio
The price-to-earnings (P/E) ratio compares a company's current share price to its earnings per share.

Return
Ratio of outgoing payments to incoming payments of an investment.

Stoxx 600
Share index of European companies from the large, mid and small cap segment.

S&P 500
Index weighted by market capitalisation that represents the 500 leading listed companies in the U.S.

Value Stocks
Stocks that are characterized by a favorable valuation, high book value and a solid equity ratio.

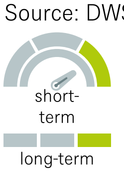
Yield Curve
Graphically displays the interest rates of bonds with different maturities.

Legend

The strategic view by September 2025

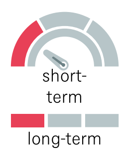
The indicators signal whether DWS expects the asset class in question to develop upwards, sideways or downwards. They indicate both the short-term and the long-term expected earnings potential for investors.

Source: DWS Investment GmbH; CIO Office, as of 06 November 2024



Positive return potential

Potential profits but also risk of loss rather limited



Negative return potential

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