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Chief Investment Office GWM
Investment Research

Buy on dips in equities

Prepare for market volatility

Author: Sagar Khandelwal, Strategist, UBS Switzerland AG

- **Why?** (1) Fed interest rate cuts in non-recession periods have historically been favorable for equities. (2) We believe exposure to artificial intelligence will prove key to long-term portfolio growth. (3) Phasing-in strategies can help investors manage near-term volatility while capturing longer-term gains.
- **Why now?** (1) We expect the S&P 500 to rise to 6,600 by year-end and to 6,800 by June 2026. (2) Moderate investor positioning and robust realized earnings growth suggest to us that markets are not in a bubble. (3) US technology, health care, utilities, and financials; select Asian markets; and quality and thematic opportunities in Europe all offer attractive growth prospects, in our view.

We think that investors underallocated to stocks should consider phasing strategies and/or prepare to add exposure on potential market dips.

We believe the equity bull market remains intact and expect an economic soft landing, solid corporate earnings, and lower interest rates to support markets over the next 12 months. We see opportunities across regions:

US: Technology, health care, utilities, and financials
In the US, we expect the strongest performance to come from the technology, health care, utilities, and financial sectors:

Technology: In the short term, we believe that investors need to be mindful of the risk of a period of "capex indigestion," as incremental revenue growth continues to lag incremental capex growth at big tech companies. However, over the medium and longer term, exposure to AI will prove essential to long-term portfolio growth, in our view. Underlying consumer and business use of AI is already outpacing expectations, and AI solution providers are making good progress converting usage into revenue. We believe that the scope to monetize will expand further, and we remain confident that technology companies will ultimately earn an attractive return on the investments they are currently making.

Health care: The pharmaceutical industry faces significant uncertainty not only from tariffs but also from Trump's push for Most Favored Nation (MFN) drug pricing, although much of the potential negative consequences of these two policy risks is already priced in. Resolution of these two policy overhangs should materially improve sentiment and provide a meaningful valuation lift. We continue to rate the US health care sector as Attractive. Promising new therapies in large, untapped markets—such as obesity and Alzheimer's—should help offset patent expirations.

Utilities: The sector's defensive characteristics should offer ballast in a portfolio if economic growth slows further. In addition, roughly 20-25% of the sector has material exposure to AI power demand.

Financials: Easing regulation, early signs of a pick-up in capital market activity, and improving net interest margins should support a recovery. Ongoing growth in payments, driven by digital adoption and robust transaction volumes, adds further momentum. We believe these positive trends, alongside solid fundamentals, position the sector well for the months ahead.

Asia: Singapore, India, and China's tech sector

Singapore: Singapore stands out as a relative "safe haven," backed by its strong currency, high dividend yields, and local equity market reforms. Easing trade tensions also bode well for its trade-reliant economy. For global investors, the market offers high dividend yields and currency diversification benefits.

India: We continue to believe the current elevated US tariffs on India are unlikely to be permanent in nature, and there is scope for India to offer concessions. While the Indian equity market could remain volatile in the near term, its relatively closed economy and its lower dependence on exports will likely help blunt the economic impact. We believe Indian equities will be driven by double-digit earnings growth over the next two years, and we expect private consumption and government spending to continue to support the economy.

China tech: We continue to favor China's tech sector, which is supported by new advancements, growing AI adoption, bottom-up fundamental improvements, and domestic policy support. The sector's valuations are still reasonable, earnings growth is expected to be strong (~20% for 2025E), and currency appreciation could provide a further lift. We prefer leading names in online gaming, cloud services, and online travel agencies.

Europe: Quality, industrials, and thematic plays

Six ways to invest in Europe: The increasing hope of a ceasefire and peace between Russia and Ukraine could lead to improving consumer, business, and market sentiment across Europe, as well as some benefits through lower energy prices and a focus on rebuilding Ukraine. A potential easing of Russian sanctions could add additional upside to equity markets. There are still many unknowns, however, and we recommend our "Six ways to invest in Europe" theme, which selectively includes some of the beneficiaries of a potential truce. Other key trends in the region include market volatility, policy shifts in Germany, and increased defense and cybersecurity spending.

Swiss high-quality dividends and income strategies: We think Swiss dividend-paying equities are attractive, as the average dividend yield, at around 3%, is higher than that of Swiss franc bond yields. With robust balance sheets and profitability, we think this suggests that market-wide distributions are sustainable.

European quality: We rate European quality stocks as Attractive, as we see an appealing entry point. These companies' strong profitability, resilient earnings, and solid balance sheets make them well suited to a late-cycle, volatile environment. Historically, quality stocks have outperformed during periods of slow growth and uncertainty, and much of the direct tariff risk now appears priced in. We see a compelling risk-reward for broad-based exposure.

European industrials: We hold a positive outlook on European industrials given the long-term structural growth and near-term catalysts. The sector trades at a forward P/E discount to US industrials, offers structural growth exposure to our Power and resources theme, and would benefit from reshoring manufacturing and materially higher European defense equipment spending. In addition, the sector should benefit from a pick-up in global manufacturing activity, supported by an end of destocking in China—an important end-market for several large European industrials.

Brazil: Still constructive

Brazil is a relatively closed economy, with exports to the US representing less than 2% of GDP. The direct impact on economic activity and corporate earnings from tariffs will likely be contained, and Brazilian stocks should continue to be supported by a weaker US dollar, ongoing interest in geographic diversification by global investors, improving corporate returns on equity, and the prospect of central bank rate cuts.

Appendix

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