Source: UBS

Solid earnings season supports equity markets

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Despite political turmoil, the medium-term market trend remains determined by fundamentals, with global earnings growth of over 12% in 4Q24. Investors should seize opportunities in the US, small- and mid-cap European stocks, and select emerging markets.

While markets are currently being shaken by political tremors with an epicenter in Washington D.C., it should not be overlooked that the medium-term trend is still primarily determined by fundamentals, particularly corporate profits. We therefore believe it is important to closely follow the key events of the ongoing 4Q24 earnings season.

Almost three quarters of companies in the US and Japan, half of those in Europe, and a quarter in emerging markets have reported so far. Earnings surprises are above average in Japan and the US, Europe is near average, and emerging markets have missed expectations. Global earnings growth rose to 12.4% year on year in 4Q24, the highest level since mid-2022. The technology, consumer discretionary, and materials sectors show particularly solid earnings growth. In the US, S&P 500 earnings growth is around 13% year on year, the strongest in three years. Europe, on the other hand, recorded a decline of 2.7%, while Japan and emerging markets posted strong growth of 24% and 16%, respectively.

Revenue growth is strong in all regions, with margins near record levels in the US and Japan, but falling in Europe and the emerging markets. Although consensus estimates for the first quarter of 2025 have been lowered for virtually all major markets, double-digit earnings growth is expected for the US, Japan, and the emerging markets in 2025, with growth in the mid-single digits in Europe.

Despite the ongoing announcements surrounding the escalating tariff and trade conflict, we believe the fundamental backdrop remains positive. Uncertainty about US trade and fiscal policy, inflation and the pace of monetary easing by the US Federal Reserve will continue to cause market fluctuations. However, tariffs on Canada and Mexico are unlikely to be permanent, if at all, and solid US economic growth should provide a tailwind for equities. The gradual Fed rate cuts are also positive for equities. Artificial intelligence (AI) is likely to remain an important driver of equity market returns for several more years. We believe equities have further upside potential and expect the S&P 500 to rise to 6,600 by December 2025. Otherwise, we see opportunities in Asia ex-Japan, including Taiwan and India. We also prefer eurozone small- and mid-cap stocks, the health care sector, and high-quality dividend stocks in Switzerland. Investors who are underinvested in AI can use periods of volatility to get add exposure. Structured strategies with capital protection features can help manage market volatility while staying invested.

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