While CIO remains positive on global equities supported by resilient US growth and AI tailwinds, a smooth journey up is unlikely. (UBS)

Prepare for an increase in stock volatility

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News headlines have been fast-moving this year, especially since Donald Trump returned to the White House just over a month ago. One may be surprised, though, to find that the VIX index of implied US equity volatility has stayed below its long-term average of 20 since late December.

In fact, the index's current level is not far from the lowest point following the US presidential election. But volatility is potentially one asset class that is mispriced, in our view, especially given the potential political, geopolitical, and technological shifts that are likely to unfold in the months ahead.

More tariff plans are expected to be unveiled, with some going into effect. Aside from the additional 10% tariffs imposed on Chinese imports earlier this month, most of President Trump's proposed tariffs have yet to be enacted. We don't think all tariff plans will be followed through given the potential damage they may cause to US growth and inflation, but we have said investors should prepare for aggressive US trade policies. Markets may need to adjust their pricing of the tariff impact as more detailed plans or new proposals are revealed in the coming weeks and months.

US government shutdown risk and budget reconciliation could trigger volatility. US Congress is struggling to strike a deal to keep the government funded before the 14 March deadline to prevent a shutdown, as top appropriators have yet to agree on a figure for the 12 annual funding bills. In addition, the budget reconciliation process in April is likely to trigger market volatility as Republicans, with their slim majority, look to pass various pieces of legislation that were promised on the campaign trail.

Geopolitical uncertainties remain elevated. President Trump's call with Russian President Putin last week and comments on his Ukrainian counterpart Zelenskiy marked a surprise turn in the war in Ukraine. We think the market is currently partially pricing in rapid progress toward a ceasefire, but the path is by no means certain. We do not rule out the possibility of further escalation in the war, which could lead to negative shocks for markets. Meanwhile, in the Middle East, it remains to be seen whether a second phase of the Gaza ceasefire can be negotiated once the initial stage concludes at the end of this month.

So, while we remain positive on global equities supported by resilient US growth and AI tailwinds, a smooth journey up is unlikely. Investors should ensure portfolio diversification and consider hedging tools such as capital preservation and volatility-selling strategies.

Click here for more details on our global equity strategy.

Original report: **Prepare for an increase in stock volatility amid (geo)political shifts, 21 February 2025.**

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