



Morgan Stanley Global Macro Forum

After the Sell-Off – Our Current Stance on Markets and the Economy

March 17, 2025

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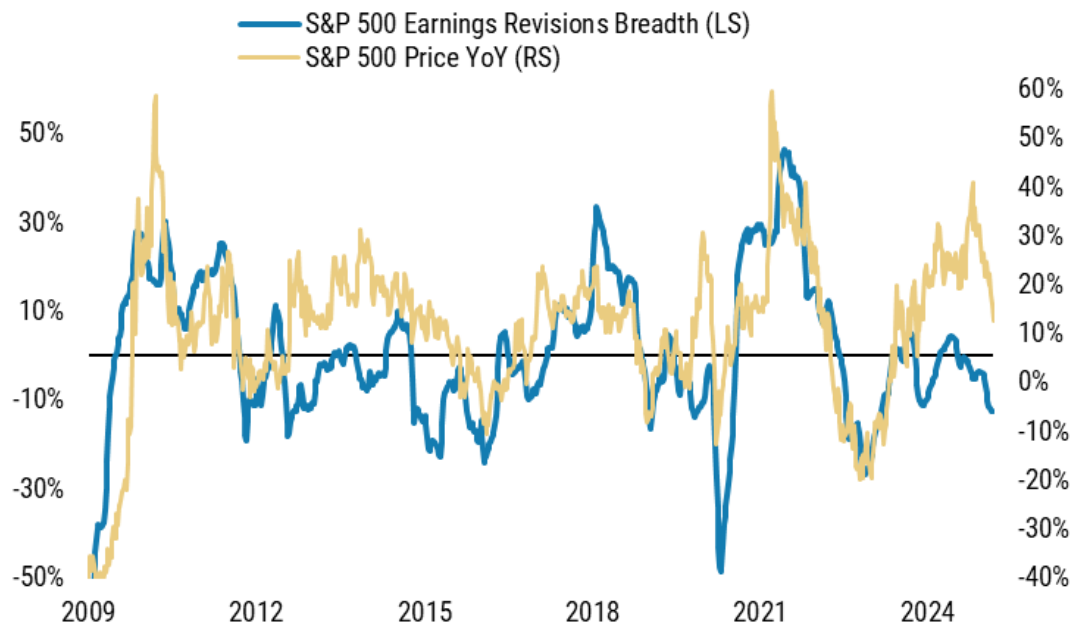
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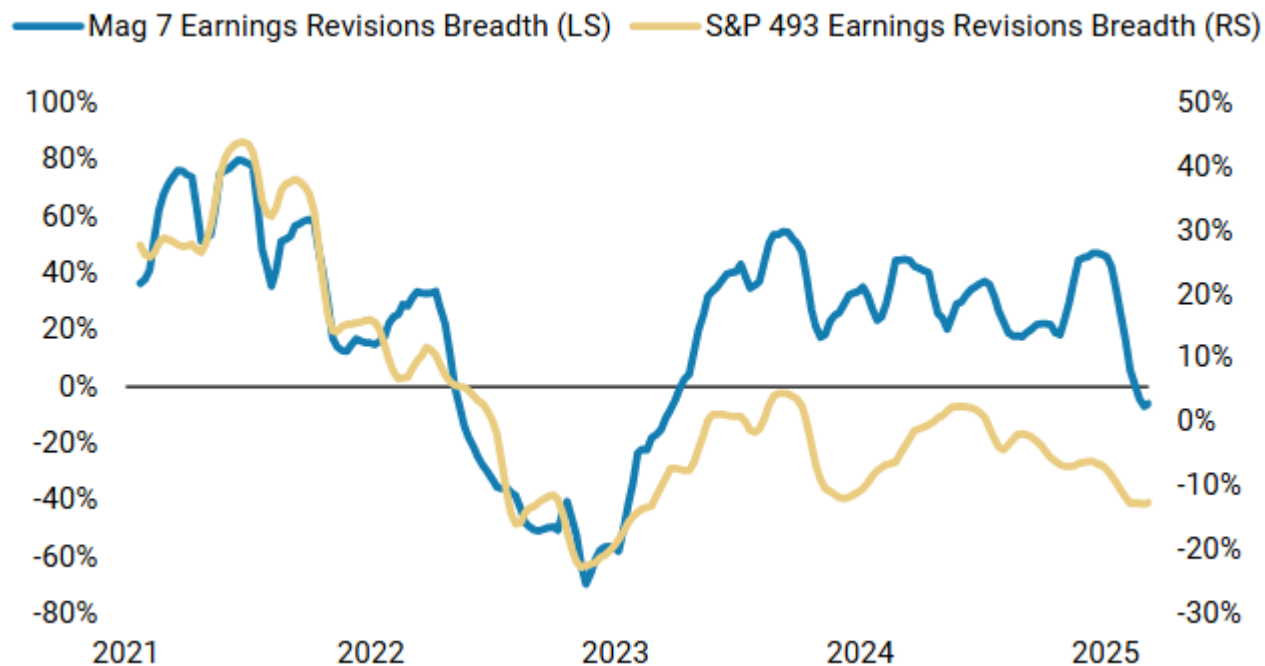
Chief Investment Officer and Chief US Equity Strategist

Earnings Revisions Rolled Over in Early December, Long Before Policy Changes Were Implemented or Feared....



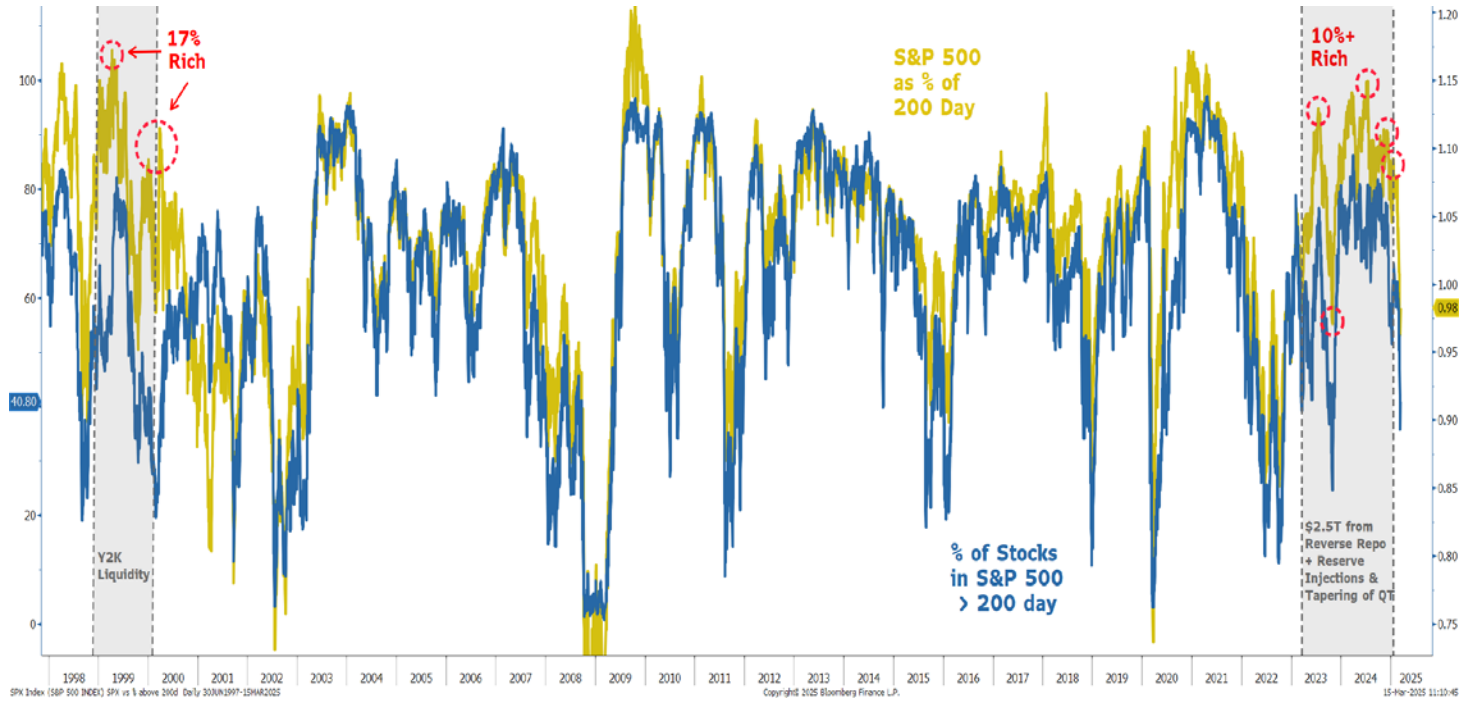
Source: FactSet, Morgan Stanley Research

...and the Revisions Have Been Led by the 'Magnificent 7'



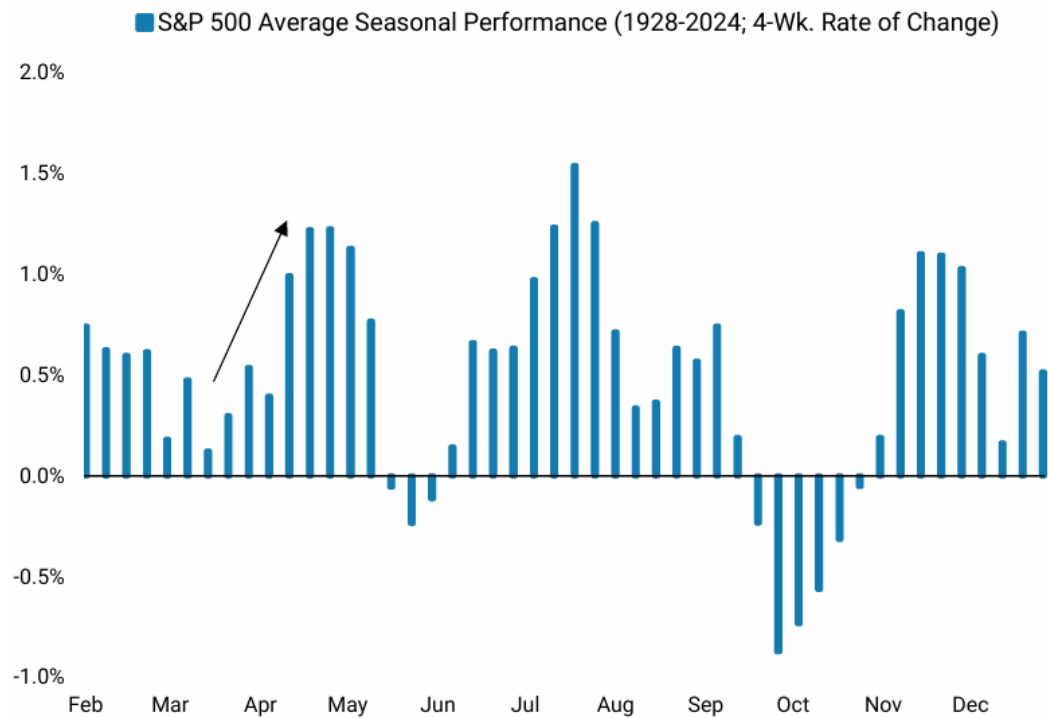
Source: FactSet, Morgan Stanley Research

Market Breadth Very Weak and Different than Last Summer....Short-Term Buy Signal but Another Headwind in the Medium Term



Source: Bloomberg, Morgan Stanley Research

Seasonality Could Also Support a Short-Term Rally



Source: Bloomberg, Morgan Stanley Research

Quality Has Been the Clear Leader Since the End of 2021. Why?



Source: Refinitiv, Morgan Stanley Research

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Andrew Sheets

Global Head of Credit Research

Don't Misread Credit "Resilience"

Credit has held up better. But as worries turn to growth, that matters more.

The market has been dealing with a progression of concerns, not all of which matter equally to credit:

1. Greater uncertainty lowers corporate 'animal spirits' ➡ Fine for credit ('conservatism' is good)



2. Reduced upside leads to a momentum unwind ➡ Fine for credit (low issuer overlap)



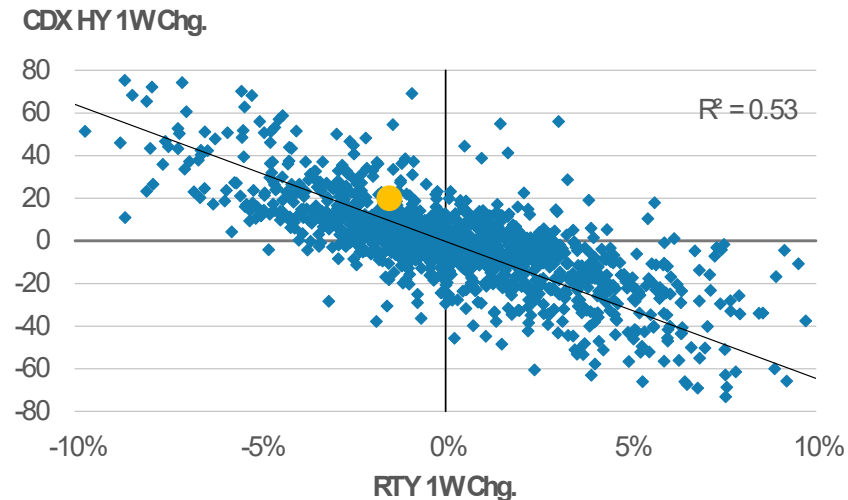
3. Lower expected growth, stickier inflation and less easing ➡ Bad for credit

And 'Resilience' Has Been Weakening

Last week, credit actually lagged...

HY spreads underperformed small caps

CDX.HY vs. Russell 2000 Monthly Changes



European HY also underperformed

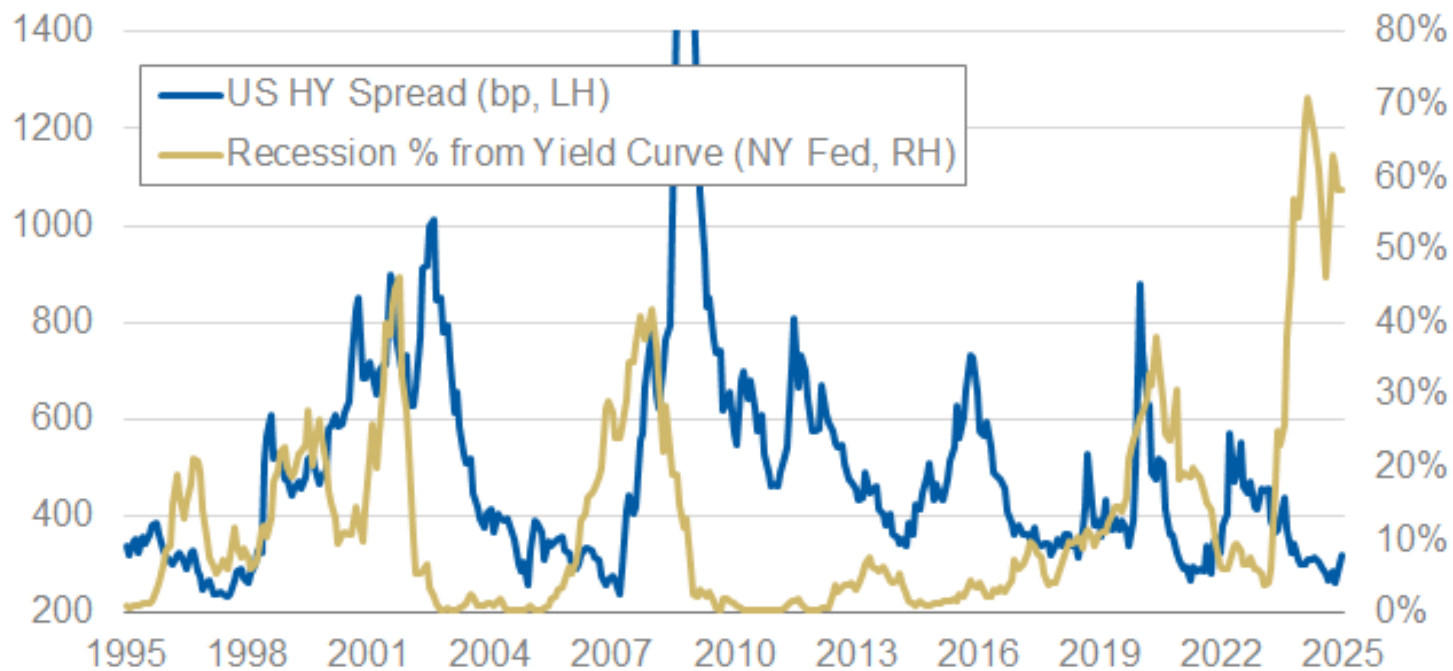
iTraxx XOver vs. SX5E Monthly Changes



Source: Bloomberg, Morgan Stanley Research

Use Any 'Bounce' to Upgrade Quality, Reset Index Hedges

'Beta' in credit doesn't pay well. Look to reset hedges post March 20 'roll'.



Source: Bloomberg, Morgan Stanley Research

Morgan Stanley

Vishwanath Tirupattur
Chief Fixed Income Strategist

Key Takeaways

- **Economics:** Divergence continues to be a theme; we revised up the growth forecast for Europe while revising down the forecast for the US for the first time in years. Despite the shift in German fiscal policy, the euro area output gap should remain negative, and inflation will likely undershoot. The ECB will have to cut rates below neutral. Risks to US growth are skewed to the downside. Markets have generally taken the right macro signals, but some caution in extrapolation is needed.
- **Rates views:** Germany's bond issuance is set to surge in 2026, driving volatility in yields and ASW. Supply risks for 2025 seem contained, but markets have overshot on duration and ASW levels relative to issuance dynamics. Expect lower yields and a steeper curve ahead in Bunds. Investors will look to how the Fed characterizes the growth versus inflation trade-off and how it compares to market prices – which increasingly focus on growth. We suggest investors remain defensive in their macro positioning and recommend long government bond duration in the US and the UK.
- **FX views:** We stay bearish on USD, driven by expectations for a weaker US economy and an improvement in growth expectations in the eurozone. We focus our bearish USD view on the DXY (long EUR/USD, short USD/JPY), given risks that lower US growth and/or tariff escalation impact global sentiment, putting downward pressure on EM and commodity FX.
- **US equities views:** With the S&P trading at the low end of our 1H range, a tradable rally is likely. Sentiment/positioning are lighter, seasonality is improving and the DXY/10Y yield are down 6%/50bp over the last two months. This doesn't mean growth risks are extinguished. Volatility is likely to persist in 2025.
- **Credit views:** In the medium term, the backdrop for credit is getting worse – slower growth and stickier inflation with a potentially less responsive Fed. These risks pose a rising risk to credit's 'resilience'. Use any near-term respite to improve quality, move into lower dollar-price bonds and add index hedges post the March 20 roll.

Valuation Methodology and Risks

Trade	Entry Level	Entry Date	Rationale	Risks
Short USD/JPY	156.2	16-Jan-25	USD/JPY should fall alongside declining US interest rates given the high sensitivity of the pair to rates and rate differentials.	US rates rising thanks to stickier inflation or stronger US data, fueling a rally in USD/JPY.
Long EUR/USD	1.028	16-Jan-25	EUR/USD should see gains as US rates fall, supporting risk appetite and bolstering the currency pair closer to its rate differential-implied fair value.	Trade tensions escalate meaningfully between the US and Europe.

Source: Morgan Stanley Research

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(as of February 28, 2025)

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	Count	% of Total	Count	% of Total IBC	% of Rating Category	Count	% of Total Other MISC
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Equal-weight/Hold	1694	45%	370	45%	22%	810	47%
Not-Rated/Hold	3	0%	0	0%	0%	0	0%
Underweight/Sell	601	16%	83	10%	14%	230	13%
Total	3,794		831			1735	

Data include common stock and ADRs currently assigned ratings. Investment Banking Clients are companies from whom Morgan Stanley received investment banking compensation in the last 12 months. Due to rounding off of decimals, the percentages provided in the "% of total" column may not add up to exactly 100 percent.

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