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FEBRUARY 27, 2025

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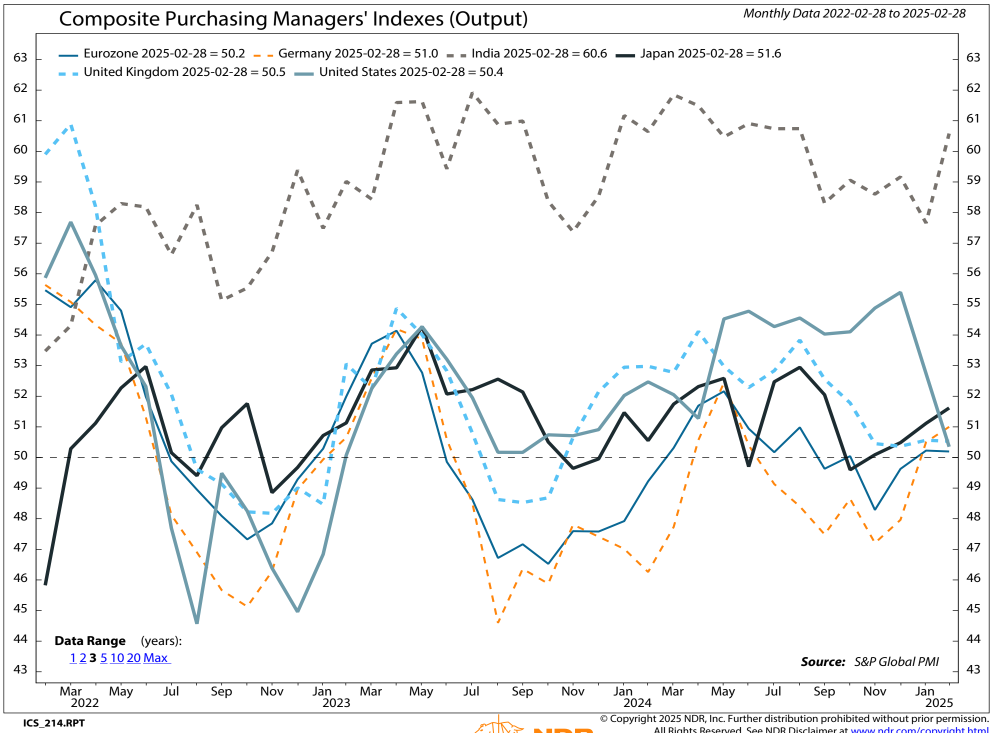
Is the international economy finally starting to show relative strength?

Key Takeaways

- Directionally, the U.S. economy may be taking a break, while data in other parts of the world appears to be looking up.
- Historically, U.S. equities have tended to underperform during these periods of relative economic underperformance.
- But with the U.S. being so economically and financially integrated with the rest of the world, an immense decoupling cannot last.

International PMIs have done better since the start of the year



U.S. exceptionalism

The U.S. economy has been exceptional for several years. As we noted in the November 1 Hotline, U.S. economic growth since the pandemic has far superseded that of any other major developed economy.

While several cyclical factors were at play, along with greater resistance to tighter monetary policy, potential real GDP growth in the U.S. is significantly greater due to faster productivity and better demographic prospects.

No longer?

Unless something dramatic happens, it would take years to break that mold, with the U.S. still expected to continue to clock in real GDP growth rates much higher than its developed economy counterparts.

However, directionally, the U.S. economy may be taking a break, while data in other parts of the world appears to be looking up at the start of the year. As we noted in Friday's Daily Economic Perspectives, the flash composite PMIs outside of the U.S. showed relatively more constructive performance, continuing that trend from January (see chart above). Additionally, most international Citigroup economic surprise indexes are positive, while economic surprises in the U.S. have turned negative.

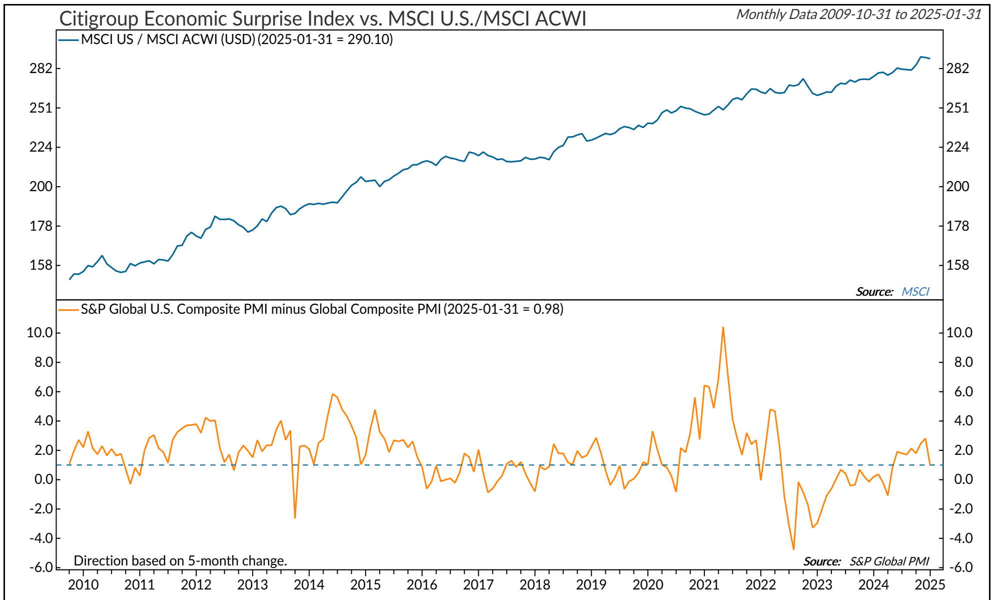
Historically, U.S. equities have tended to underperform during these periods of relative economic underperformance, using those two data series as a metric.

But with the U.S. being so economically and financially integrated with the rest of the world, an immense decoupling cannot last. As of now, recession risk remains quite low in the U.S., suggesting a more benign outlook. But we continue to watch the risks.

The U.S. composite PMI has typically been higher than the global average. While that was still the case in January, the gap closed to the least since early 2024. We do not have a global composite PMI reading for February yet, but the economies that reported flash PMIs for the month, including the U.S., suggest the gap likely narrowed further this month.

As shown in the chart at right, instances like this have seen U.S. equities rise less on a relative strength basis.

Falling U.S. PMI vs. global has seen U.S. equity R/S underperform



Returns Regardless of Direction
MSCI U.S./MSCI ACWI Performance
Chart View: 2010-03-31 to 2025-01-31

U.S. PMI minus Global PMI	% Gain/ Annum	% of Time
Above 1.0	5.36	64.06
Below 1.0	2.12	35.94

Buy/Hold = 4.18% Gain/Annum

U.S. PMI minus Global PMI Rising
MSCI U.S./MSCI ACWI Performance
Chart View: 2010-03-31 to 2025-01-31

U.S. PMI minus Global PMI	% Gain/ Annum	% of Time
Above 1.0	6.03	42.73
Below 1.0	5.37	10.68

Buy/Hold = 4.18% Gain/Annum

U.S. PMI minus Global PMI Falling
MSCI U.S./MSCI ACWI Performance
Chart View: 2010-03-31 to 2025-01-31

U.S. PMI minus Global PMI	% Gain/ Annum	% of Time
Above 1.0	4.03	21.33
Below 1.0	0.77	25.26

Buy/Hold = 4.18% Gain/Annum

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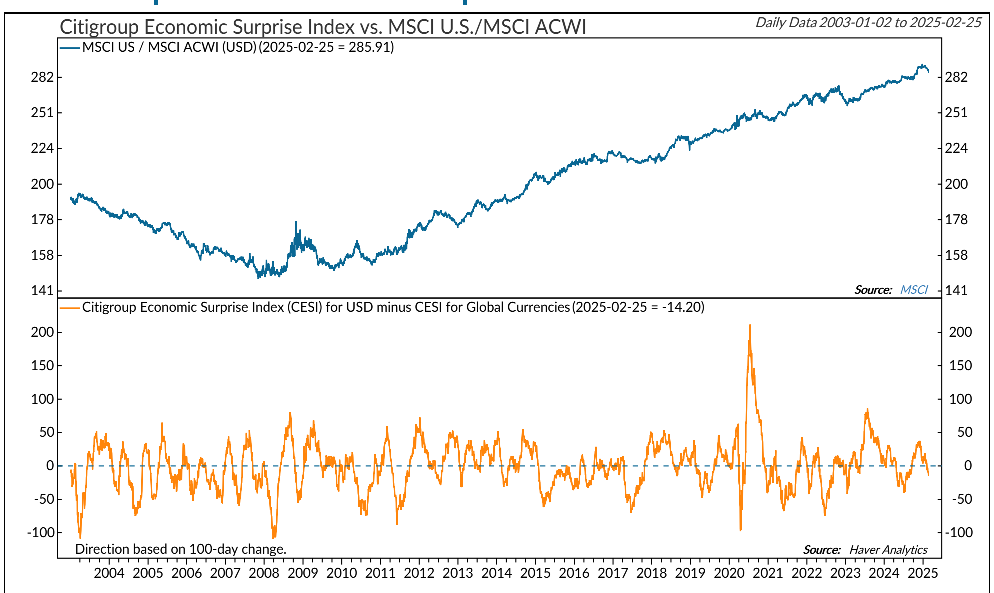
A similar picture with the surprise indexes



Returns Regardless of Direction
MSCI U.S./MSCI ACWI Performance
Chart View: 2003-05-22 to 2025-02-25

USD CESI minus Global CESI	% Gain/ Annum	% of Time
Above 0.0	2.72	51.43
Below 0.0	1.01	48.57

Buy/Hold = 1.89% Gain/Annum

USD CESI minus Global CESI Rising
MSCI U.S./MSCI ACWI Performance
Chart View: 2003-05-22 to 2025-02-25

USD CESI minus Global CESI	% Gain/ Annum	% of Time
Above 0.0	3.18	37.33
Below 0.0	-1.05	11.66

Buy/Hold = 1.89% Gain/Annum

USD CESI minus Global CESI Falling
MSCI U.S./MSCI ACWI Performance
Chart View: 2003-05-22 to 2025-02-25

USD CESI minus Global CESI	% Gain/ Annum	% of Time
Above 0.0	1.76	14.05
Below 0.0	1.67	36.87

Buy/Hold = 1.89% Gain/Annum

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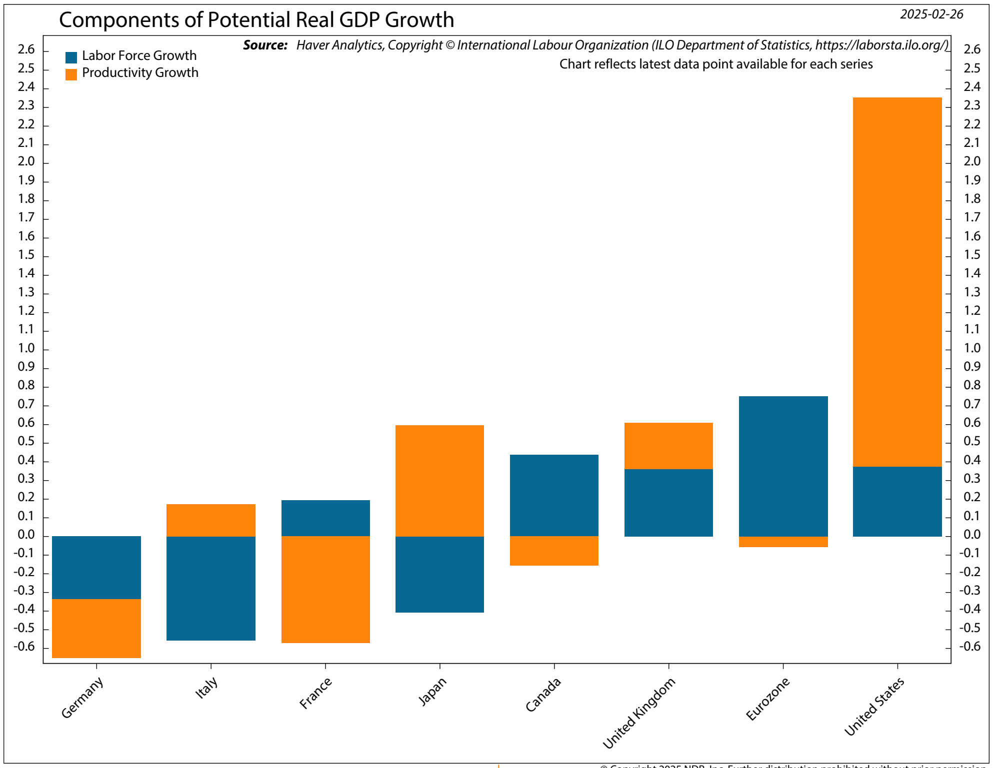
In addition to the PMIs, most data on balance have been surprising to the upside internationally over the past months, including in the eurozone, Japan, Canada, and the U.K. In some of the economies, easier monetary policy and reduced domestic political risk have contributed to their rosier outlooks.

In the U.S., however, surprises have turned net negative. Seasonal adjustment issues, colder-than-normal weather, and the L.A. wildfires may have contributed to weakness in January data. But, as evident in more recent consumers surveys, domestic political uncertainty is also playing a role.

U.S. potential growth is the fastest in the G7

The chart at right compares potential real GDP growth among major developed economies. To compile the number, we add up long-term productivity and labor force growth. No other economy comes close to growing as quickly as the U.S. on a sustainable basis.



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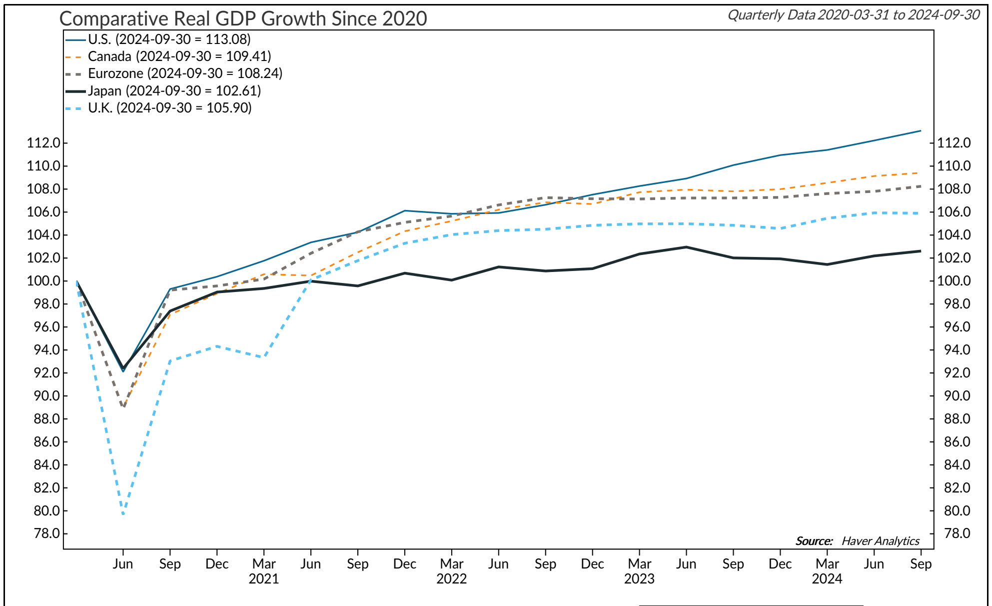
Helping it grow the most since the pandemic



Real GDP Growth 2020-03-31 to 2024-09-30	Gain/ Annum
U.S.	2.8%
Canada	2.0%
Eurozone	1.8%
Japan	0.6%
U.K.	1.3%

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Due in part to this, the U.S. economy has expanded much faster in recent years.

Most of the world's economies are very integrated with the U.S.

Sustained decoupling from the U.S. economy is nearly impossible. The table at right, extracted from report ICS_272, shows the correlations of PMIs all over the world. Most of the world is tightly integrated with the U.S. economy. We show the correlations with China, the world's second largest economy, for sake of comparison.

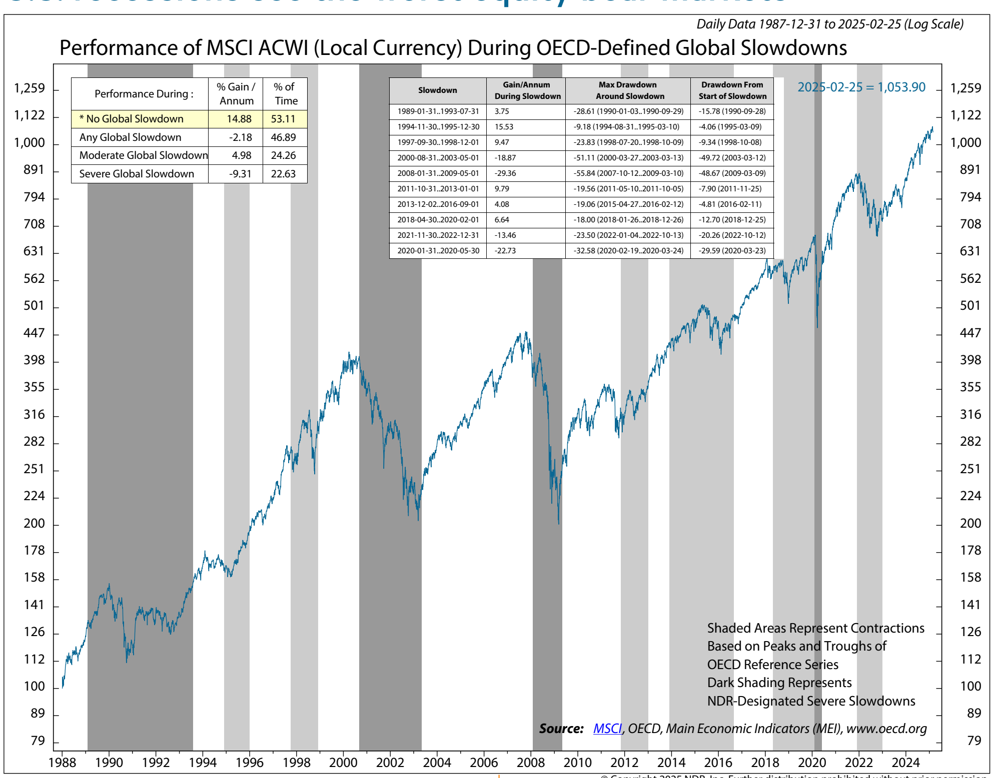
S&P Global Purchasing Managers' Index (PMI) Correlations by Economy

	China	United States
Global	0.36	0.81
Global ex China	-0.15	0.94
Global ex Eurozone	0.47	0.79
Global ex Japan	0.34	0.83
Global ex U.S.	0.72	0.32

Source: S&P Global PMI

Ned Davis Research — excerpt from ICS_272.RPT

U.S. recessions see the worst equity bear markets



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Given the U.S.'s widespread financial integration, equity bear markets associated with U.S. recessions tend to be far worse than those associated with slowdowns emanating from elsewhere. The good news is that U.S. recession risk remains low for now.

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Economic Summary Report for the World

- **Report:** ICS_250_GLBL.RPT
- **Run Date:** 2025-02-26
- Download Chart Bundle

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Economic Activity | Economic Sentiment | Inflation | Inflation Surveys | Debt

Green = Improving, Red = Worsening, (Download Economic Activity Chart Bundle)

Title	Value	Units	Monthly % Change	Quarterly % Change	Year-to-Year % Change	Date	Compare Globally
Manufacturing PMI[1]	50.1 (33.8 / 57.6)	Index	0.5 (-7.7 / 5.5)	0.7 (-11.3 / 11.0)	0.1 (-18.1 / 20.9)	2025-01-31	ICS_212
Services PMI[1]	52.2 (23.5 / 63.8)	Index	-1.6 (-13.0 / 12.8)	-0.9 (-29.3 / 27.3)	-0.2 (-29.5 / 33.4)	2025-01-31	ICS_213
Composite PMI[1]	51.8 (26.0 / 62.8)	Index	-0.8 (-12.9 / 11.5)	-0.5 (-26.2 / 25.1)	-0.1 (-26.3 / 30.6)	2025-01-31	ICS_214
PMI: Capacity Utilization[1]	49.7 (38.7 / 60.9)	Index	0.4 (-3.1 / 5.1)	0.0 (-6.7 / 6.4)	0.3 (-12.3 / 15.0)	2025-01-31	N/A
Share of Manufacturing PMIs Above 50[1]	47.2 (0.0 / 100.0)	%	5.6 (-41.2 / 27.8)	5.6 (-67.3 / 66.7)	8.3 (-96.3 / 92.3)	2025-01-31	N/A
OECD Composite Leading Indicator for G20 Economies[1]	100.4 (89.6 / 104.7)	Index	0.1 (-4.7 / 3.7)	0.3 (-9.7 / 8.5)	0.6 (-9.7 / 11.8)	2025-01-31	ICS_200
Share of OECD CLIs Above 100[1]	82.4 (0.0 / 100.0)	%	5.9 (-50.0 / 37.5)	0.0 (-100.0 / 66.7)	52.9 (-100.0 / 100.0)	2025-01-31	N/A
OECD Area Unemployment Rate[1]	4.9 (8.8 / 4.8)	%	0.0 (3.2 / -0.6)	0.0 (3.5 / -1.1)	0.0 (3.3 / -2.2)	2024-12-31	ICS_204
Real GDP	26.3 (17.0 / 26.3)	Trillion Chained USD	N/A	1.8 (-8.3 / 11.3)	4.6 (-10.6 / 23.7)	2024-09-30	N/A
Global Economic Conditions Indicator[1]	41.9 (-417.7 / 134.4)	Index (bp)	24.8 (-308.1 / 422.6)	24.6 (-376.6 / 492.2)	23.2 (-420.8 / 552.0)	2025-01-31	N/A
Industrial Production	107.6 (46.4 / 107.6)	Index	0.8 (-8.4 / 4.6)	1.5 (-8.5 / 9.5)	2.5 (-12.8 / 17.7)	2024-12-31	N/A
Global Industrial Commodity Market Activity Index[1,2]	-45.4 (-161.5 / 189.3)	Index	-34.0 (-100.2 / 84.9)	-58.6 (-217.1 / 112.3)	-84.6 (-256.5 / 177.4)	2024-12-31	N/A
World Trade Volume	105.8 (26.5 / 105.8)	Index	1.1 (-12.1 / 7.4)	1.4 (-16.9 / 15.2)	3.3 (-19.9 / 25.9)	2024-12-31	N/A
Tanker 12-Month Time Charter Rate	51.5 (16.0 / 100.0)	Thous. USD/day	-3.7 (-35.8 / 88.2)	33.8 (-54.4 / 100.0)	35.5 (-65.7 / 207.7)	2025-02-28	N/A
Drewry WCI Composite Container Freight Benchmark	2,794.8 (658.2 / 10,377.2)	USD/FEU	-18.9 (-41.9 / 148.3)	-18.8 (-60.2 / 190.7)	-25.1 (-80.5 / 367.8)	2025-02-20	N/A
Contex Index	1,419.0 (237.0 / 3,578.0)	Index	-0.6 (-48.6 / 43.4)	3.4 (-72.5 / 107.9)	101.3 (-79.4 / 668.6)	2025-02-25	N/A
Global House Price Index	189.8 (99.3 / 189.8)	Index	N/A	0.6 (-0.5 / 4.0)	3.1 (-0.5 / 16.0)	2024-09-30	N/A

Sources

- Bank for International Settlements, Long series on credit to the private non-financial sector
- Fearnleys.com
- Food and Agriculture Organization of the United Nations, www.fao.org
- Haver Analytics
- OECD, Main Economic Indicators (MEI), www.oecd.org
- S&P Global PMI
- The Hamburg Shipbrokers Association

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NDR HOUSE VIEWS (Updated February 13, 2025)

For global asset allocation, NDR recommends an overweight allocation to stocks, marketweight allocation to cash, and an underweight allocation to bonds. Our recommendations are in line with our Global Balanced Account Model.

Equity Allocation

U.S. | Our U.S. asset allocation recommendation is 70% stocks (15% overweight), 25% bonds (10% underweight), and 5% cash (5% underweight). On an absolute basis, we are overweight the S&P 500 (year-end 2025 target of 6600). We are neutral on small-caps versus large-caps (implicit overweight to mid-caps) and neutral on Growth versus Value.

INTERNATIONAL | We are overweight the United States, Canada, and Pacific ex-Japan; underweight Emerging Markets, the U.K., and Japan; and makeweight Europe ex. U.K.

Macro

ECONOMY | The global economy has shown notable resilience, with recession chances waning. Risks include monetary and fiscal policy uncertainty, a potential global trade war, sticky inflation, and easing Chinese growth.

FIXED INCOME | We remain 100% of benchmark duration, and are neutral on the yield curve. We are overweight MBS and underweight CMBS and ABS. We are marketweight everything else.

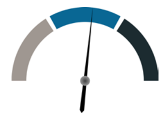
GOLD | We are currently bullish.

CURRENCIES | We are neutral on the U.S. dollar, euro, yen and the U.K. pound.

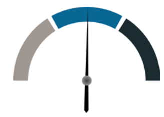
Economic Summary

February 24, 2025

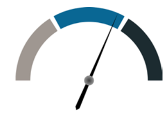
Near term activity: ● Accelerating ● Neutral ● Decelerating



Global Economy
(3.1%)



U.S. Economy
(2.0% - 2.5%)



U.S. Inflation
(2.75% - 3.25%)

Economic gauges reflect changes in near-term economic activity. Numbers in parenthesis refer to NDR 2025 forecasts.

Global Asset Allocation

● Overweight ● Marketweight ● Underweight

- Stocks (70%)
- Cash (10%)
- Bonds (20%)

Benchmark: Stocks (55%), Bonds (35%), Cash (10%)

Equities — Regional Relative Allocation

- United States 69% | Canada (5%) | Pacific ex. Japan (4%)
- Europe ex. U.K. (13%)
- Emerging Markets (5%) | U.K. (2%) | Japan (2%)

Benchmark – U.S. (64.0%), Europe ex. U.K. (11.7%), Emerging Markets (10.2%), Japan (5.3%), U.K. (3.4%), Pacific ex. Japan (2.5%), Canada (2.8%)

Global Bond Allocation

- Europe (35%)
- U.S. (56%) | U.K. (4%)
- Japan (5%)

Benchmark: U.S. (57%), Europe (27%), Japan (12%), U.K. (5%)

U.S. Allocation

- Stocks (70%) | Mid-Cap
- Small-Cap | Large-Cap | Growth | Value
- Bonds (25%) | Cash (5%)

Benchmark: Stocks (55%), Bonds (35%), Cash (10%)

Sectors

- Financials (16%)
- Materials (1%) | Real Estate (1%)

Benchmark: Technology (30.5%), Health Care (11.5%), Financials (12.8%), Communication Services (9.4%), Consumer Discretionary (10.7%), Consumer Staples (6.4%), Industrials (8.5%), Energy (3.5%), Utilities (2.3%), Real Estate (2.2%), Materials (2.2%)

U.S. Bonds — 100% of Benchmark Duration

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See the Signals.™

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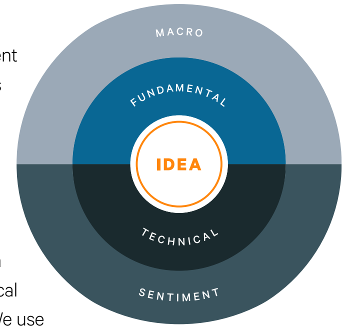

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