Level Set — A Disconnect and An Opportunity

US GDP Is Slowing

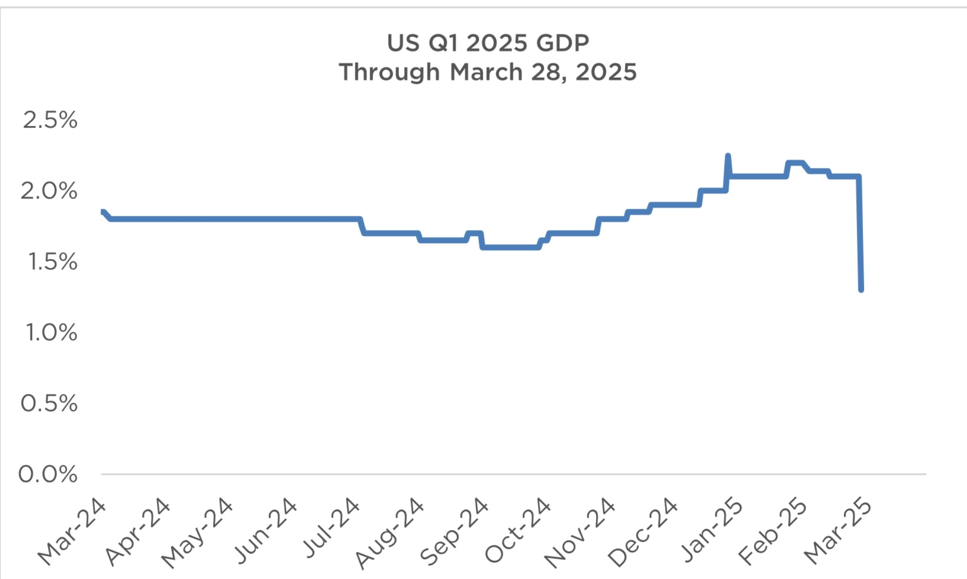
The spike in the VIX and the market sell-off this past week is not surprising in our view. While many were calling for a tactical bounce in risk-taking, we have learned that making short-term market calls is a fool's game. Our primary concern for the market is that we see a high probability of negative pre-releases during the next two weeks. Moreover, most of the economists at the major firms have lowered their GDP forecasts this year.

On Friday, according to a survey of 85 economists from March 21 to March 26 conducted by Bloomberg News:

- Q1 2025 GDP forecast at +1.2% q/q annualized versus prior survey +2.2% (see below).
- Q2 2025 GDP forecast at +1.5% q/q annualized versus prior survey +2%

This sharp reduction in the short-term outlook is likely consistent with the lower and more volatile equity market we have seen this quarter.

Q1 GDP Expectations Are Now Much Lower



Source: Trivariate Research, LP, ECGDUS Q1 2025 Bloomberg

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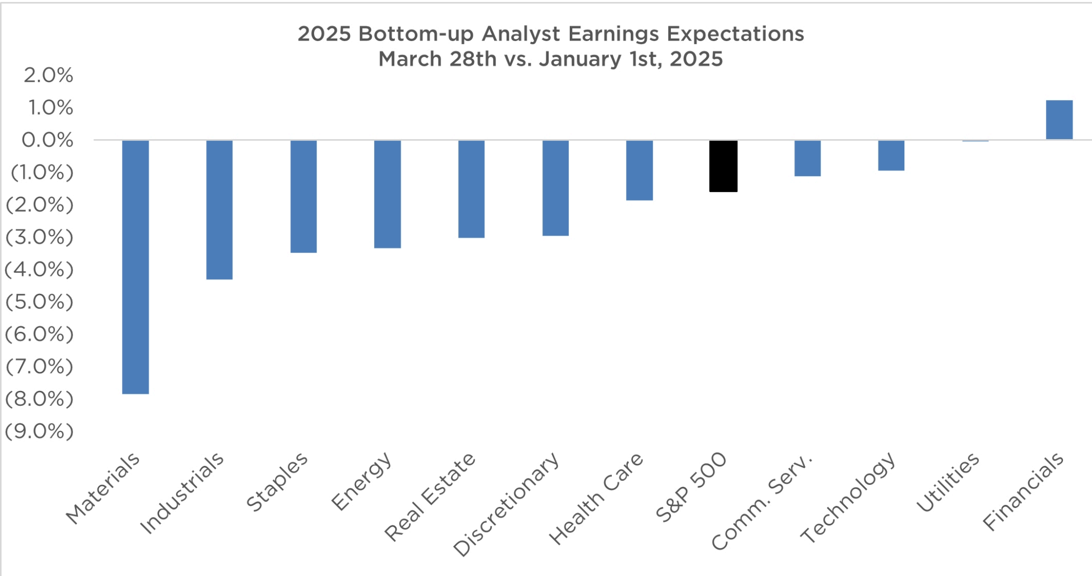
But EPS Estimates Have Only Modestly Been Revised

At the same time however, there has not been a commensurate reset in the bottom-up analysts earnings expectations for 2025, with S&P500 expectations only 1.6% lower for the full year now than they were on January 1st (see below). Expectations have been reset the most in Materials and Industrials, but are higher for Financials now than they were to start the year.

Analyst Earnings Expectations for 2025 Are Only 1.6% Lower

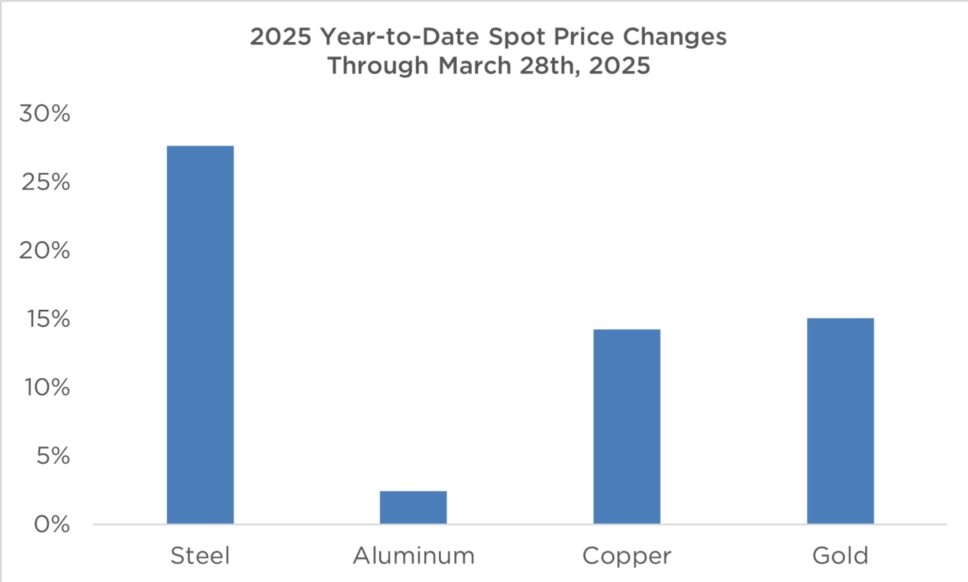


Source: Trivariate Research, LP

As we head into April next week, we continue to believe that the risk-reward is skewed to the negative for the S&P500. We expect either some negative pre-releases in the second half of this week, and / or poor guidance during April reporting season, as the economic outlook and earnings outlook look too disconnected in our view. Importantly, we have not yet seen any evidence that the stocks of companies guiding down or missing estimates are performing well, indicating that lower expectations are not "in the price."

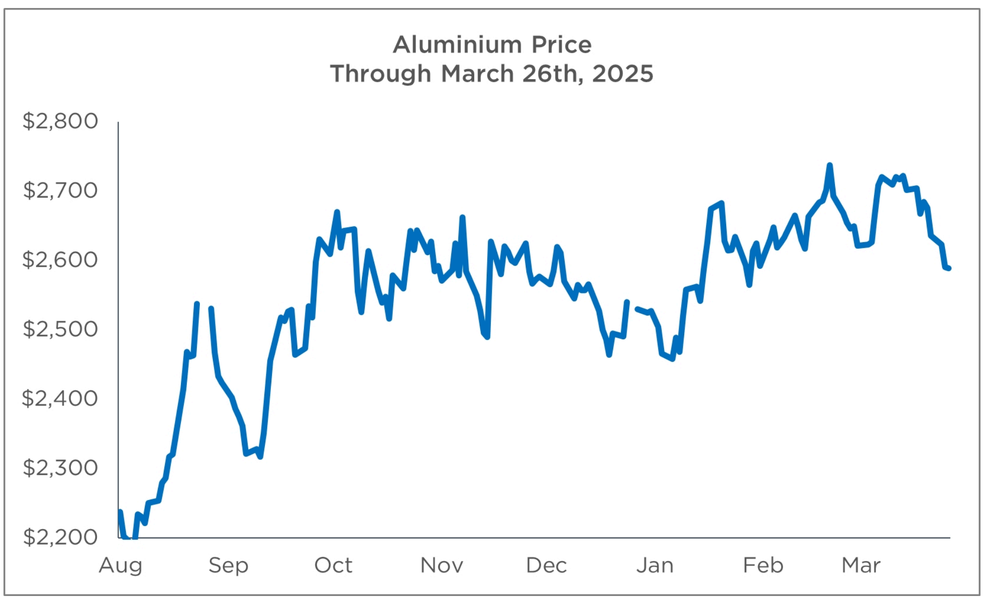
We continue to think the estimates for Healthcare are more achievable than other parts of the market, which is partly our rationale for this sector being our top pick.

But, this week, we heard a tariff-related pitch from an investor that really resonated with us. It was a pitch to own US-focused Metals. Most of the major metal spot prices are up year-to-date (see below), meaning these companies should have above average estimate achievability as spot prices and their earnings are highly correlated. We think investors should have a goal heading into earnings season of avoiding companies with poor relative revisions and owning those with better relative revisions. Through that lens, Metals stocks are looking incrementally attractive. Steel, Copper, and Gold prices are all up year-to-date, which would not have been our default assumption in a world when the economy and GDP forecasts are slowing (see below).



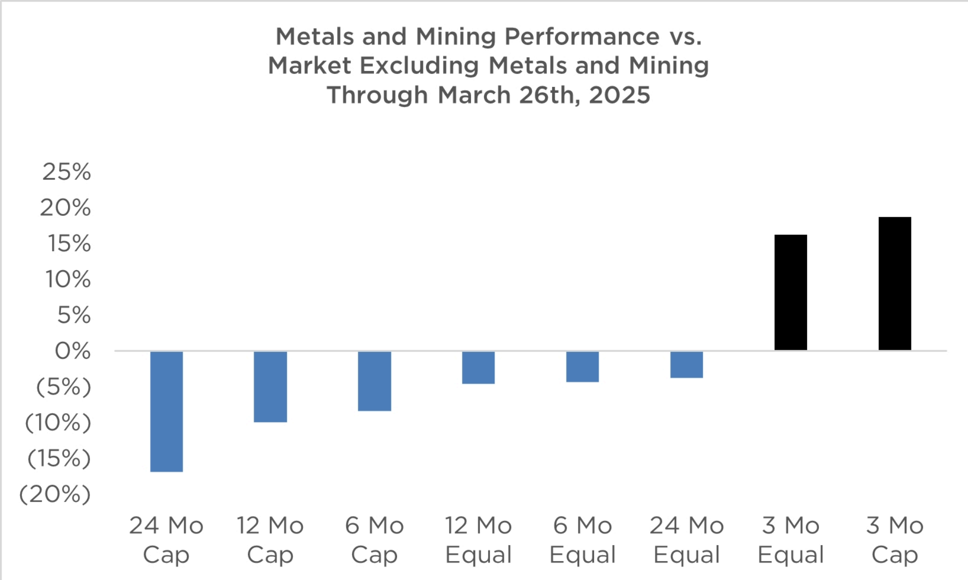
Source: Trivariate Research, LP

While Aluminum has been up the least year-to-date, the US produces quite a small amount of Aluminum relative to its total consumption and this Administration's goal in part appears to be to make sure the US is not excessively reliant on China and other countries for Metals and Materials. Aluminum has been trending higher since Trump's probability of winning started to grow last Fall, but tariffs clearly benefit US-centric companies. The tariffs have yet to impact reported results. The US produces less than 1% of the world's Aluminum, but consumes closer to its GDP percentage, meaning it is extremely reliant on China and Canada, the 1st and 4th largest producers to supply Aluminum for finished good consumption. Century Aluminum (Ticker: CENX) and Alcoa (Ticker: AA) are the two stocks in our database with the highest correlation to changes in the Aluminum prices.



Source: Trivariate Research, LP

The Metals and Mining stocks have outperformed over the last three months (see black bars below) but still have a long way to go before catching up on a relative basis for longer horizons. We think the combination of relative strong 3-month momentum and relatively more achievable earnings estimates makes for good risk-reward heading into April, unlike many other areas of the market.



Source: Trivariate Research, LP

CONCLUSION: We like Healthcare, and we like Metals and Mining heading into April earnings, as both seem to have above average estimate achievability.

Important Disclosures

Analyst Certification

The analysts, Adam Parker, Maxwell Arnold, Chang Ge, Colin Cooney and Ryan McGovern, responsible for the preparation of this research report certifies that: all the views expressed in this research report accurately reflect the research analyst's personal views.

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