

**MacroSpotlight**

**In-depth coverage on specific assets, markets, or thematic topics. Explore trends, challenges, and opportunities**

**Will US Exceptionalism continue to be reflected in 2025 Returns?**

**Qi's MFERM reveals a stronger start for RoW factor returns**

**Quant insight**

In this note, we ask if US exceptionalism is at risk and explore the scope for RoW outperformance. Applying Qi's macro factor equity risk model (MFERM), we highlight that the YTD attributable macro factor returns of EEM and EFA have been higher than SPY. We reveal the macro drivers of that relative factor return outperformance.

**First, a series of facts to provide context:**

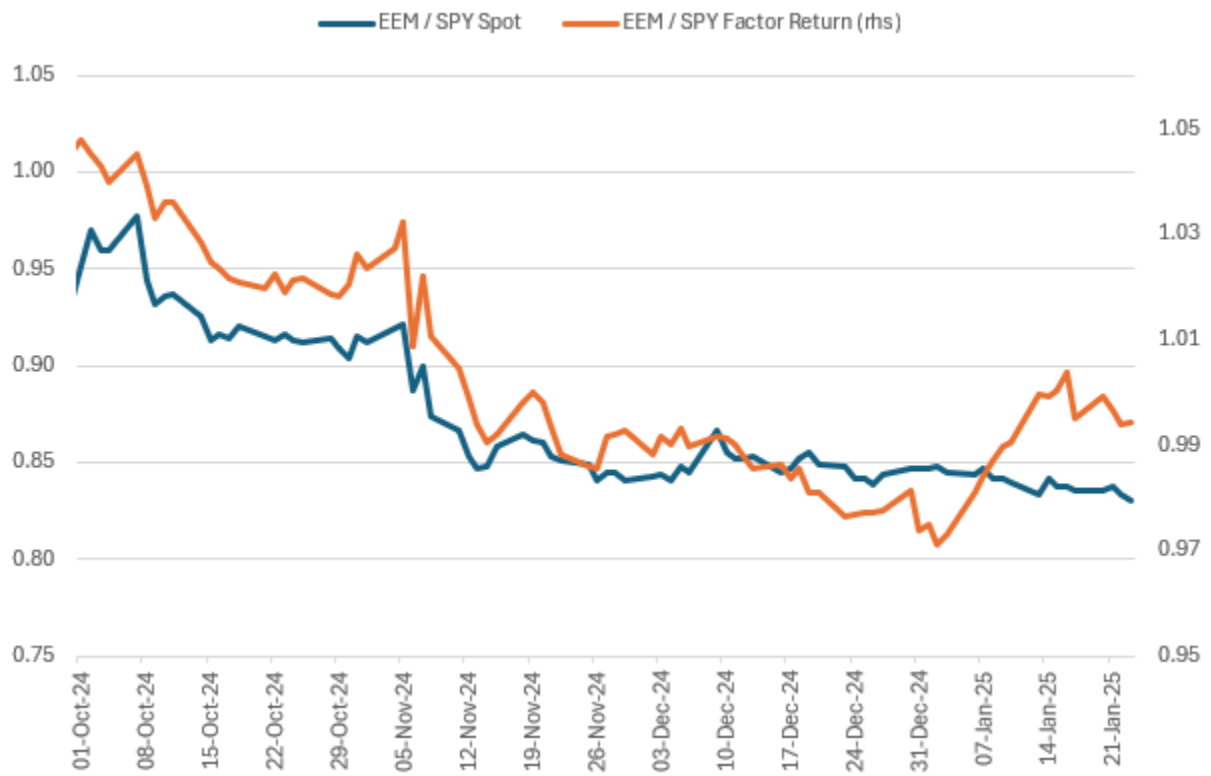
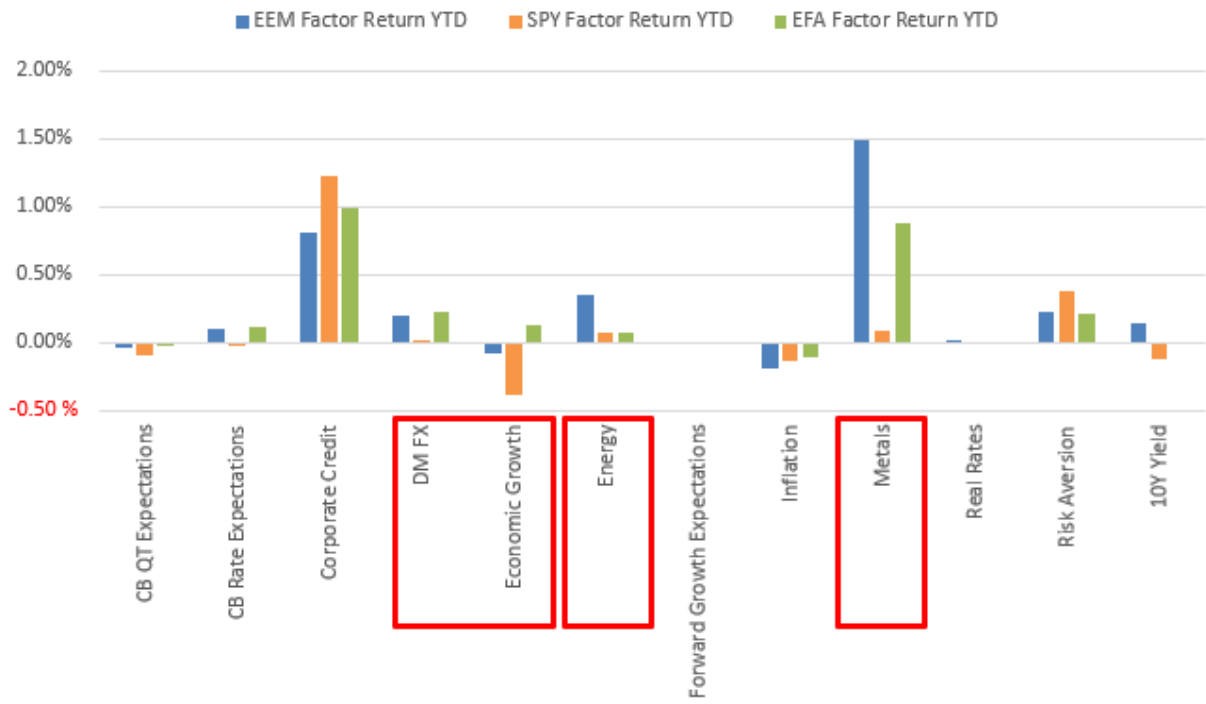
- Foreigners own a historical record amount of US equities: ~30% of total equity market cap.
- FXI, the Chinese large cap ETF returned 29% in 2024, outperforming SPY for the first time in 7yrs. China is investable despite what commentators say.
- Technically, the US bull market started in 2023 following the >20% correction in 2022. Incidentally, soon after the release of ChatGPT in Nov22. History may not repeat but the third year of a bull market is associated with single digit returns.
- The S&P500 equity risk premium is at 20yr lows (proxied by the index earnings yield relative to 10yr risk free).
- The current Republican majority in Congress is one of the slimmest in history.
- Scott Bessent has an objective to boost US GDP growth to 3% while at the same time reduce the budget deficit from 6% to 3%. The Atlanta Fed GDP nowcast is already today at ~3%.
- The Eurozone and Japan composite PMIs are now >50.
- DeepSeek, the Chinese developed LLM, has achieved competitive results with significantly fewer resources than its global competitors. It has also taken a more open-source approach.

**Given the above, a series of observations and conjectures:**

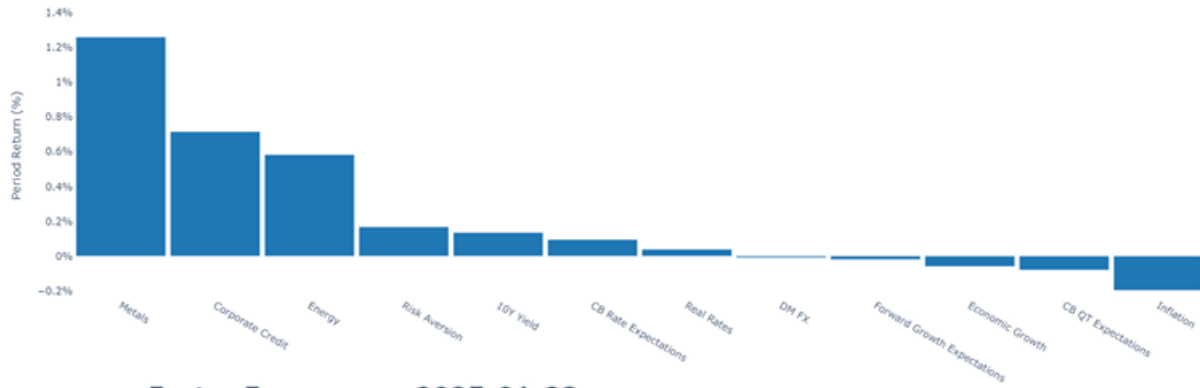
- US equities are priced for perfection, the RoW is not – The S&P500 has outperformed MSCI World ex US by >400% since the GFC.
- If we are in a single digit US equity return world, RoW has room to outperform. Consider that when the US is up 20% no one cares about RoW. When the US is down 20%, you sell everything. So in a single digit return world, do we have room for RoW?
- Is Trump actually a catalyst for RoW to act more forcefully on fiscal policy? Will the German elections unlock the debt brake? China has substantial room to act fiscally. Japan is world's largest holder of treasuries after China. There is risk of further repatriation to drive their domestic agenda.
- Is peace in Ukraine bearish Europe or actually bullish?
- Successful execution of Bessent's 3 arrows is a tough ask given the slim majority and deficit target.
- Are we at peak Trump vibes with the launch and subsequent sell off of Trump / Melania coin?
- DeepSeek's innovation questions the return on the huge AI capex of the US Tech MegaCaps. It is willing to share its breakthroughs and therefore a potential disruptor to US AI.
- US equities may well do fine in 2025 but if US exceptionalism is questioned RoW will outperform...in the words of Wayne Gretzky, skate to where the puck is going.

**So what to look for? To be right on the above, the dollar must weaken and commodities rally.**

**What does Qi's macro factor equity risk model show?** The attributable factor return of EEM and EFA (ie. the return trajectory based purely on macro drivers) have been rising YTD relative to SPY. Why? The top driver is the 7% rally in copper YTD. The weaker dollar, stronger economic growth and higher WTI have also allowed for relative factor return strength. See the series of charts below.

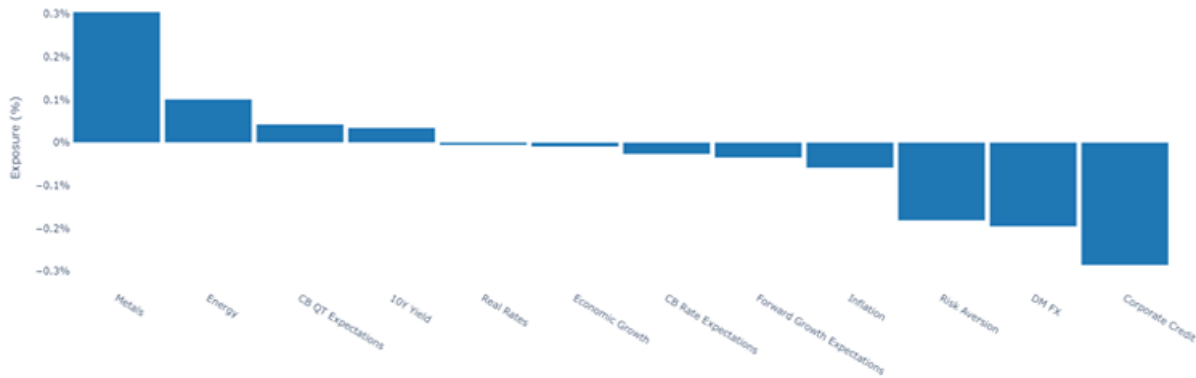


## eem: Factor Return Attribution (%) - 2024-12-23 to 2025-01-23



## eem: Factor Exposures - 2025-01-23

(% Change for 1std daily move higher in factor)



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