CIO thinks the fundamental backdrop remains supportive for equities, driven by solid economic and earnings growth, likely interest rate cuts, and rising investment in AI. (UBS)

Can equities rally from all-time highs?

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The S&P 500 has recovered from its April pullback, setting a new all-time high in May. While a range of economic and geopolitical risks remain, we think solid economic and earnings growth, the prospect of lower interest rates, and rising investment in AI should create a supportive backdrop for equities for the rest of this year.

CIO continues to favor quality stocks, including the US IT sector.

The S&P 500 has rallied to a new all-time high in May.

- As of 17 May, the S&P 500 was up 11% year-to-date. The index has set 23 record-closing highs so far this year.
- A strong first-quarter earnings season and signs of a soft landing for the US economy have boosted equities.
- Valuations are not cheap, with the S&P 500 trading on around 20 times forward price to earnings.

But we think the fundamental backdrop remains supportive for stocks.

- US economic growth remains solid, and we expect inflation to continue its gradual downward trend amid declines in rents and a moderation in wage growth.
- The Fed is on track to cut interest rates this year, most likely starting in September.
- We expect earnings growth of 9% for the S&P 500 in 2024. In our view, the 1Q earnings season underlined that the investment case for AI remains intact.

We are constructive on equities and favor quality stocks, including technology.

- We expect AI-related companies to drive strong earnings growth in the years ahead, and recommend investors to hold a healthy strategic allocation to tech stocks.
- Investors looking to diversify beyond tech can consider alternative growth themes like the low-carbon transition, healthtech, and the ocean economy. We also see value in small- and mid-cap stocks.
- At a country level, we like UK equities based on our positive views on oil and industrial metals.

Did you know ?

- Historically, record highs have not been a barrier to further stock market gains. Over the past 60 years, in the one-, two-, and three-year periods following a new all-time high, S&P 500 returns have averaged 12%, 23%, and 39%, respectively. This is hardly different from the 12%, 25%, and 38% average returns for all other periods over the same time frames.
- Structured strategies can help investors position for further upside while protecting against downside, or earn income while awaiting a potentially better entry point.
- Companies with "quality" attributes typically have strong returns on invested capital, resilient operating margins, and relatively low debt on their balance sheets.

Investment view

We see a supportive backdrop for equities, and favor opportunities in quality stocks, including technology. We think investors should hold a diversified, strategic exposure to the tech sector while remaining mindful of concentration risks. For those diversifying beyond technology, we see opportunities in alternative growth themes (e.g., the low-carbon transition, healthtech, and the ocean economy) and in small- and mid-cap stocks.

Main contributors - Vincent Heaney, Alison Parums, Daisy Tseng

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