Yardeni Research

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Morning Briefing

Concentration
Here & There

Check out the accompanying chart collection.

Executive Summary: Much ink has been spilled on the Magnificent-7 stocks' outsized influence over the S&P 500's performance given the group's huge share of the index's capitalization. Are other stock markets of the world similarly weighed down (or buoyed up) by a few corporate behemoths? … That is the case for several stock markets in Asia, William reports, but not Japan's. … Melissa discusses the European Union's "steady giants," which weigh in collectively at a hefty one-fifth of the EU MSCI's capitalization and actually have outperformed the Mag-7 since 2022. … And Joe shares data on the Mag-7's fluctuating share of the S&P 500's capitalization in recent months.

Asia Strategy I: High Time Asian Markets Diversified. "What's good for Samsung is good for Korea." This maxim, riffing off CEO Charles Erwin Wilson's observation about General Motors and America in the 1950s, has become even truer over time in Asia's *fourth-biggest economy*.

They don't call South Korea "*The Republic of Samsung*" for nothing. Founded in 1938, the sprawling conglomerate is often credited for South Korea's rise from one of the globe's poorest nations in the 1950s to the thriving tech power it is today and for the global appeal of the *$1.8 trillion* Korea Exchange.

Yet Samsung's *20% share* of the KOSPI index leaves Korea Inc. in something of a tail-wagging-the-dog dilemma. What's more, at the start of 2024, the combined sales of Korea's top four family-controlled groups, or "*chaebols*," generated nearly *41% of the nation's GDP*. The four: Samsung, SK Hynix, Hyundai Motor, and LG. Consider the following:

(1) *A broader problem*. Korea isn't the only top economy in Asia confronting a market-concentration problem that puts the fate of any one bourse in very few hands. Taiwan is an even more extreme case.

Taiwan Semiconductor Manufacturing Company (TSMC) wields a *68% market share* of the Taiwan Stock Exchange (TWSE). Understandably, TSMC, with its *trillion-dollar* market capitalization, is the pride of the tech-heavy island economy. The globe's biggest and most advanced semiconductor foundry is the top supplier for Apple Inc. and Nvidia Corp. Its dominance makes TSMC an obvious crown jewel in the power struggle between the US and China.

(2) *Taiwan's extreme example*. But TSMC is also Exhibit A not only for the risks of sectoral concentration in an economy—chips, in this case—but also for increased market volatility. Where TSMC goes on a particular day, so goes the broader *TWSE Capitalization Weighted Stock Index*. This limits diversification opportunities for investors seeking broader market exposure. And increases risk if, say, geopolitical intrigue comes for TSMC.

In an October 17, 2024 *earnings call*, Morgan Stanley's Charlie Chan asked the TSMC brass how they might "handle the potential antitrust risk, given your near monopoly," saying he's "a little bit concerned, same as other investors." TSMC executives, including CEO C.C. Wei, seemed surprised by the query and pivoted to other issues.

Market dominance is a challenge shared by TSMC's top customers as well. Nvidia recently *drew the attention* of US antitrust regulators, while Apple routinely confronts regulators' antitrust questions in the US, European Union (EU), *Japan*, and beyond. Such is life in the trillion-dollar valuation club, where the travails of one company can quickly destabilize the broader market.

(3) *The China factor*. China also finds itself listed among countries with stock markets where the 10 largest names collectively constitute a 50% or greater share of the broad index's capitalization. Other major economies on that list—besides Korea and Taiwan—include: Brazil, France, and Germany.

In Taiwan's case, the index is dominated by TSMC, Hon Hai Precision (Foxconn), MediaTek, Quanta, and Fubon. In Korea, it's Samsung, SK Hynix, KB Financial, Hyundai Motor and Naver.

In China, the market-swaying giants are Tencent, Alibaba, and Meituan. As Morningstar points out in a *January report*, "China's market concentration has shifted from 'old economy' companies to 'new economy' players like Tencent, Alibaba, and Meituan. Despite their dominance, regulatory challenges and economic headwinds have weighed on performance. For instance, Alibaba's stock has more than halved over the past five years due to regulatory scrutiny and a weak consumption environment."

Asia Strategy II: Japan's Good Example. Japan's equities market stands out as a comparatively diversified one. This may cut against the conventional wisdom, given how much global attention is focused on behemoths like Toyota, Sony, Mitsubishi UFJ Financial, and Hitachi. In a March 2024 report, Peter Oppenheimer of Goldman Sachs *called Japan* "the best diversification opportunity" among developed markets. The broader Topix, Oppenheimer argues, has nearly 2,000 companies. Here's more:

(1) *India's growing appeal*. In this regard, India fares reasonably well, too. Over the last five years, *India's weight* in the Morningstar Emerging Markets Index has doubled. The reason: *structural reforms* by Prime Minister Narendra Modi's government, which are boosting foreign investment. These upgrades helped pave the way for mid- and small-cap companies to list and grow, creating investment opportunities across *Asia's third-biggest economy*.

Yet India has a role in efforts to create an Asian version of the US's "*Magnificent-7*" (i.e., Alphabet, Amazon, Apple, Meta Platforms, Microsoft, Nvidia, and Tesla). The Asian "*Super 8*," identified by UBS, groups Korea's Samsung, Taiwan's TSMC and Hon Hai; China's Tencent and Lenovo; Japan's Tokyo Electron; India's Infosys; and Singapore's ASMPT.

(2) *Asia's 'Fantastic Four*.' Not to be outdone, Societe Generale has its own China-specific "Seven Titans" club. It includes Alibaba, BYD, JD.com, NetEase, Semiconductor Manufacturing International Corporation, Tencent, and Xiaomi. There's also China's "*Fantastic Four*" companies, which are deemed to be disrupting global tech markets and aiding Asia's biggest economy in its rivalry with the US. The four: TikTok, drone maker Da-Jiang Innovations, robot company Unitree, and AI upstart Deepseek.

Will such herding lead to even greater market concentration in China and beyond in the Asia-Pacific region? Only time will tell. But Asia would do well to broaden the leadership of its stock markets, making them less susceptible to extreme fluctuations and more appealing for long-term investment.

Europe Strategy: EU's Steady Giants. The "steady giants" of European equities may lack the flashiness and excitement of their US tech counterparts, but their solid performance warrants attention. In particular, Europe's relatively boring financial stalwarts have outperformed the Mag-7 since 2022, Joe confirms.

The EU MSCI provides investors with a diverse group of large- and mid-cap stocks. The 10 largest stocks that *anchor* the EU MSCI account for 20.0% of the index's total capitalization. This elite group mirrors Europe's low-risk but diversified equities profile, spanning sectors from Technology, Consumer Staples, and Healthcare to Financials, Energy, and Industrials. The 10 titans are: enterprise software leader SAP (index weighting, 2.6%), semiconductor equipment giant ASML (2.4%), consumer staples powerhouse Nestlé (2.3%), four pharma stalwarts—Roche (1.9%), Novartis (1.9%), AstraZeneca (1.8%), and Novo Nordisk (1.8%)—multinational banking behemoth HSBC (1.7%), key energy player Shell (1.7%), and industrial giant Siemens (1.5%).

In terms of country weightings in the EU MSCI, the prominence of the UK and Switzerland underscores the enduring strength of financial centers outside the EU, while Germany and France remain the political and industrial engines inside the EU.

Let's review some of the EU MSCI's sector concentrations and constituents before a quick look at the index's country weightings:

(1) *Financial giants don't (entirely) depend on the ECB*. Financials stocks dominate the EU MSCI, representing 22.7% of the index's market capitalization. European banks recently have faced compressed net interest margins as the European Central Bank (ECB) has lowered rates. But HSBC, despite lower *net interest margins* y/y during Q1, has maintained solid underlying profits *growth*, thanks to a focus on its wealth division and a favorable asset mix. The bank, which has been buying back its shares, has undergone a restructuring to cut costs and simplify its organizational structure.

(2) ***I**ndustrial sector growth is set to be domestically fueled***.** Industrials, representing 18.51% of the index, have *muddled along* amid soft economic growth and tepid global demand. Looking ahead, this sector will benefit from the EU's increased spending on energy infrastructure and rearmament. Siemens, the German engineering behemoth, sees limited impact from global tariffs this year and remains *confident* in its global supply-chain diversification.

(3) *Healthcare is innovating and aging well***.** Healthcare holds a 13.8% weight, led by Roche, Novartis, AstraZeneca, and Novo Nordisk in the top 10 constituent weightings. In 2025, the pharmaceutical sector will be *shaped* by AI-powered drug discovery and innovative treatment approaches. Europe's broad demographic shift toward an aging population will provide structural support to the industry in the years ahead.

(4) *Tech is strategic but not dominating.* Less than 10.0% of the index is represented by

information technology companies. Right behind SAP in the weightings is ASML, arguably one of Europe's most strategically important companies. The Dutch firm leads in extreme ultraviolet (EUV) lithography semiconductor equipment, making it indispensable to chipmakers worldwide.

(5) *Country weights are UK-heavy and Spain-light*. The EU MSCI's companies are heavily concentrated from just a handful of countries, with the UK topping the list (22.4%), followed by France (16.8%), Germany (15.6%), Switzerland (14.6%), and the Netherlands (6.9%). Together, these five nations represent more than three-quarters of the index's weight.

Notably absent from the upper tier is Spain, despite its economic importance in the region. Spain and other countries that have a small equities presence fall into the "Other" category, which has a 23.7% weighting in the EU MSCI index.

US Strategy: The Seven's Flickering Magnificence. In 2024, the Mag-7 beat the S&P 500 for the 11th time in 12 years, recording a collective market-capitalization gain of 46.3%. That's nearly double the S&P 500's 24.4% rise last year. During the last week of the year, they represented nearly a third of the index's total market capitalization, or a record-high 32.0% market-cap share. That's down to a 29.7% share currently (*Fig. 1*).

This year has been a challenging one so far for the Mag-7. The uptrend in their consensus revenue and earnings growth forecasts has slowed amid relatively high valuations. Earlier this year, investors aggressively bid down the group's capitalization into bear-market territory, but most of the lost ground has been regained. Joe shares the details below:

(1) *Rapid recovery from bear market.* The Mag-7's collective market capitalization peaked at a record-high $18.4 trillion on December 24 before tumbling 28.6% to $13.2 trillion through April 8. While it has risen 29.6% since then through Friday's close, to $17.1 trillion, it's still 7.4% below its record high and down 3.1% ytd. However, that's just a few good trading days away from surpassing the S&P 500's 1.6% ytd gain and resuming its leadership in the bull market (*Fig. 2*).

Indeed, the Mag-7's market capitalization is still in positive territory on a y/y basis, as it has been for much of the time since 2013 (*Fig. 3*). The group is up 9.2% y/y, not far behind the 10.3% gain for the S&P 500. Still that's down substantially from the 75.0% y/y performance at the end of 2023.

(2) *Slower gains to record highs in consensus forecasts.* The Mag-7 stocks' collective

forward revenues rose 15.8% during 2024 (*Fig. 4*). It's well off that strong pace so far in 2025, rising just 3.9% ytd, but to a new record high of $2.4 trillion. Their forward earnings soared 35.6% last year and has risen just 6.7% ytd (*Fig. 5*). (FYI: "Forward" revenues and earnings refers to the time-weighted average of analysts' current-year and following-year consensus estimates. The forward profit margin is calculated from forward revenues and earnings.)

The Mag-7's forward profit margin improvement last year was stunning. Their collective forward profit margin started the year at a record 21.6% and finished at a new record high of 25.4% (*Fig. 6*). It has continued to improve so far in 2025, rising to 26.0% during the June 13 week and just 0.3ppts from a record-high 26.3% during the May 2 week.

(3) *Forward revenues growth rate edging lower*. While the Mag-7's forward revenues growth estimate is down from its record high, it remains well above the S&P 500's estimate as it has since 2013. Indeed, the group's latest reading of 11.8% is still more than double the S&P 500's 5.4% forecast (*Fig. 7*).

For some perspective, the Mag-7's forward revenues forecast bottomed in early 2023 at a record low of 8.0%. That followed the release of ChatGPT just a few months earlier in November 2022, when investors were still unclear about the magnitude of AI's potential. By mid-2023, Nvidia began to epically exceed forecasts on a scale not seen since Cisco did so in the 1990s. The forward revenues growth forecast proceeded to soar 6ppts to a two-and-a-half-year high of 13.9% by the end of 2024. It since has slipped to 11.8% as of the June 13 week, but that reading remains well above the S&P 500's 5.4%.

(4) *Forward earnings growth forecasts are down markedly.* Analysts following the Mag-7 companies currently think the group will grow earnings 16.6% over the next 12 months (*Fig. 8*). That's the lowest such reading in over two years and is just 5.3ppts above the 11.3% earnings growth that analysts forecast for the S&P 500 companies in aggregate.

To place the 16.6% earnings growth currently expected over the next 12 months into perspective, it's nearly twice the record low of 8.6% in late 2021, when y/y growth comparisons hit a speed bump. But it's well below the record high of 24.6% hit during the May 24, 2024 week amid the AI capital spending boom.

Calendars

US: Tues: Retail Sales Total & Ex Autos -0.5% & 0.1%; Industrial Production 0.1%; Capacity Utilization 77.7%; Business Inventories; NAHB Housing Market Index 35; Import & Export Prices -0.5% & -0.1%. **Wed:** Housing Starts & Building Permits 1.36mu/1.43mu; MBA Mortgage Applications; Initial Claims; Fed Interest Rate Decision 4.50%; FOMC Economic Projections. (Source: FX Street)

Global: Tues: Eurozone & Germany ZEW Economic Sentiment 23.5 & 34.5; Japan Machinery Orders -6.7%; BOJ Press Conference. **Wed:** Eurozone Headline & Core CPI 1.9% & 2.3%y/y; UK Headline & Core CPI 1.9% & 2.3%y/y; UK Headline & Core CPI 3.4% & 3.6%y/y; De Guindos; Elderson; Villeroy; Knot; Escriva. (Source: FX Street)

US Economic Indicators

Regional M-PMI (*link*): The New York Fed, the first regional Fed bank to report on manufacturing activity for June, showed activity contracted at a faster pace. The *headline general business conditions* index deteriorated for the second successive month to -16.0 in June from -9.2 in May and -8.1 in April—considerably below the consensus estimate of -6.0. Both the new orders (to -14.2 from 7.0) and shipments (-7.2 from 3.5) measures moved from expansion to contraction during the month, with new orders posting the steepest decline. Inventory (0.9 from 4.8) investment slowed during the month. Meanwhile, delivery times (1.8 from 1.0) held relatively steady. *Turning to the labor market*, *employment* (4.7 from -5.1) in the manufacturing sector moved higher in June—its first positive reading since January, while the average workweek was at -1.5 during the month, showing little change in hours worked. *As for pricing*, the *prices-paid* (46.8 from 59.0) measure remained high, easing from May's level, which was the highest in more than two years, while the prices-received (26.6 from 22.9) measure accelerated slightly. *Looking ahead*, firms turned optimistic in June, with business conditions climbing 23.2 points (to 21.2 from -2.0) after turning pessimistic in April and May. The report noted: "New orders and shipments are expected to increase, and firms expect supply availability to be only slightly worse in the months ahead. Capital spending plans remained soft."

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