RATHBONES Incorporating Investec Wealth & Investment (UK)

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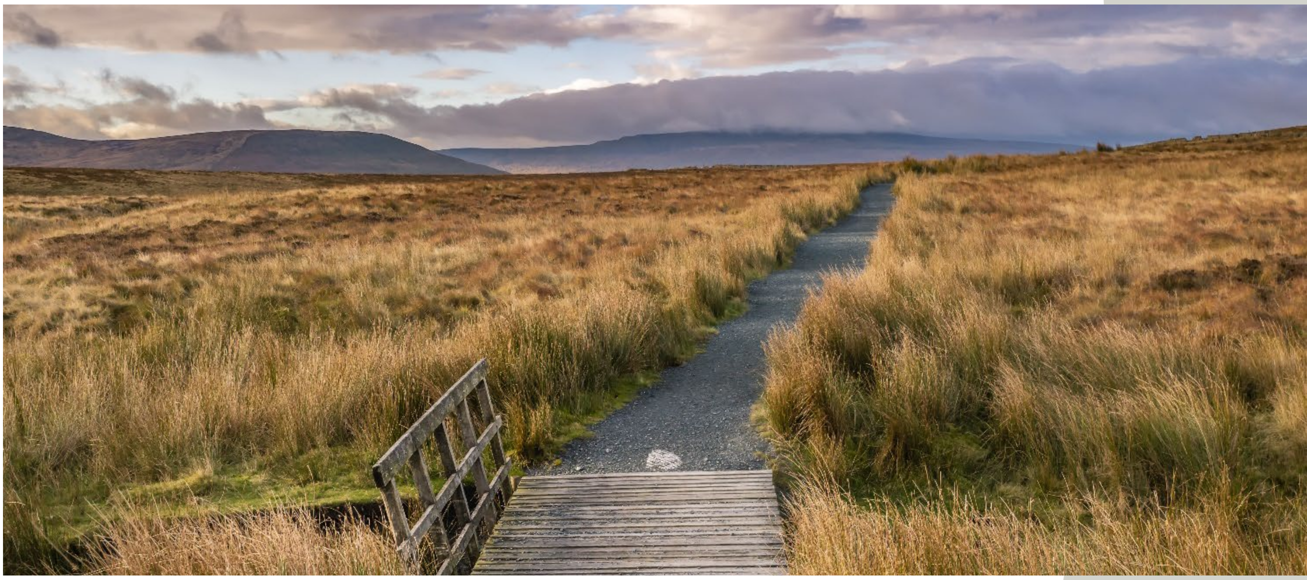
Market reflection



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Overview

Balanced portfolios made decent progress again during 2024 but there was no triumphal march towards the year end during December. As was the case for much of the last two years, investors focused on the potential paths of inflation and interest rates. The latest evidence suggests that, in the UK and US, neither are projected to continue to fall as quickly as had been hoped.

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The Bank of England held the base rate unchanged at 4.75% at its December meeting, although it hinted at potential future cuts given the weakness of the economy. In the United States, the Federal Reserve did reduce rates by another 0.25%, but lowered the number of cuts it expects for 2025 as GDP growth remains resilient and inflation above target. With investors also expressing concern about fiscal deficits, this triggered another sell-off in bond markets, creating a valuation headwind for equities. Indeed, valuation worries continue to swirl around the leading technology shares which have led US and global equity indices to new highs, as does unease at their growing share of market capitalisation. We do not believe that comparisons to the technology boom and bust at the turn of the millennium are appropriate, owing to the entrenched nature of their products and their exceptional profitability. Even so, we remain alert for signs of slowing growth and/or lower profitability which would, almost inevitably, encourage profit-taking. The focus in early 2025 will be on the transition of power in US government. Much will depend upon how aggressive returning President Donald Trump is in implementing some of his policies, notably with respect to trade tariffs and the planned reduction of the fiscal deficit through cost-cutting (to be overseen by mercurial entrepreneur Elon Musk). Following an exceptional year of risk-adjusted equity returns, we would not be surprised to find the going tougher in 2025.

- The Bloomberg consensus for World GDP growth in 2024 remains at 3.1%, up from 2.6% a year ago. The forecast for 2025 has slipped back from 3.1% to 3%. According to Bloomberg, economists estimate a 20% probability of a US recession in 2025, down from 50% at the beginning of 2024.

- Global government bonds sold off again in December, with the Bloomberg Global Aggregate dollar index falling 2.2%. This means that global bonds have delivered another year of negative total returns. The fact that this has happened when policy rates are generally falling is unusual and is the result of three factors: a degree of overoptimism at the start of the year that has been corrected; stronger (US) GDP growth and sticker inflation; and the worry about increased supply as deficits remain high and funding liabilities rise. But with yields now substantially higher than they were at the end of 2021, there is less concern about a repeat of the aggressive sell-off experienced in 2022.

- The MSCI All-Countries Index delivered a total return (TR) of 21% in 2024 in sterling, but the version excluding the US was up only 8.5%, reflecting the dominance of US equities. The S&P 500 Index returned 27%. The FTSE 100's 9% TR is respectable given its low exposure to the Technology sector and AI theme. France (-4%) was conspicuously weak thanks to a combination of domestic political turmoil and its formerly strong Luxury Goods companies succumbing to poor demand from China. But Germany's 14% rise illustrates that stock markets can diverge from weak local economies if they have exposure to strong global themes.

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