RATHBONES | Incorporating Investec Wealth & Investment (UK)

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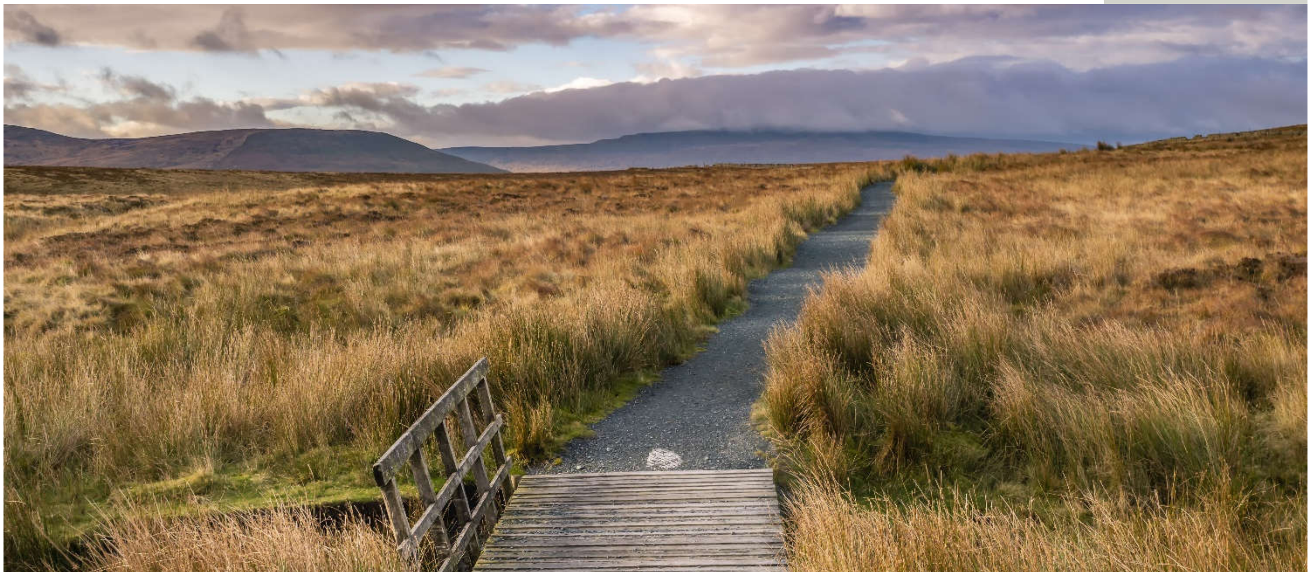
Market reflection



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Overview

If January sets the tone for the rest of 2025, we are in for an interesting and potentially volatile ride! Since the start of the year, we have had a tantrum in the bond market (leading to a sell-off in the pound); President Trump's inauguration and the chaotic policy announcements that followed; and then an upset in the Technology sector following the launch of a Chinese AI model that could disrupt the current optimistic consensus about the US tech leaders. The bond market's problems were two-fold.

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First, there were concerns in both the US and the UK that inflation was not falling fast enough to allow central banks to cut interest rates. Then, as bond yields rose, there was increasing concern that the higher interest liability on government debt might undermine solvency. The UK's position was exacerbated by the fact that a weak economy further impairs Labour's fiscal position. Yields on longer dated Gilts reached levels last seen in 1998, but that finally drew income-seeking buyers. The stress has eased for now, but the onus is on Chancellor Reeves to restore growth and confidence, possibly with a helping hand from the Bank of England. Trump's first two weeks in office have seen a flurry of executive orders, spats with Canada, Mexico, Denmark, Colombia and Panama, and a hastily reversed decision to withhold certain federal outlays. We expect more of the same. DeepSeek's launch of its R1 large language model (DSR1) threw the whole AI industry into turmoil. The effects ranged from the chipmakers and Hyperscalers through to the infrastructure providers. Our initial take is that DSR1 provides some evidence that the cost of access to AI models can be reduced, and that this is also likely to create much greater engagement and demand, following the assertion of the Jevons Paradox. We do not believe that this episode alone heralds a major setback in global equity markets, but we remain on alert.

- The Bloomberg consensus estimate for World GDP growth in 2024 is 3%, a welcome increase vs the 2.6% expected at the start of the year. The forecast for 2025 is for an unchanged 3%, and the same again in 2026. Economists estimate a 20% chance of a US recession in 2025.

- Global government bonds, having delivered another year of negative returns in 2024, started the new year on the wrong foot, with the Bloomberg Global Aggregate Index losing around 1.5% in the first two weeks before recovering into marginally positive territory. Sovereign bond auctions, despite the early scare, have continued to draw good demand at these higher yield levels and investors valued bonds' safe haven characteristics when equity markets were unsettled by the DeepSeek news. We continue to recommend a relatively short duration exposure on account of lingering inflation fears and to account for fiscal concerns.

- The MSCI All-Countries Equity Index delivered a total return (TR) of 4.5% in January in sterling, successfully negotiating the late sell-off of some of the companies that had been leading the AI charge. Nvidia lost its crown as the world's largest company, shedding $589 billion of market capitalisation in just one day, a new record, in falling 18%, although its net loss on the month was a more benign 7%.

- The FTSE 100 gained 6% (TR), boosted as much by the weaker pound as any optimism about the UK economy. The more domestically orientated FTSE 250 managed just 1% and Small Caps were unchanged. In a welcome sign of broader equity demand, European equities gained 7%.

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