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Eden Park | HRIS

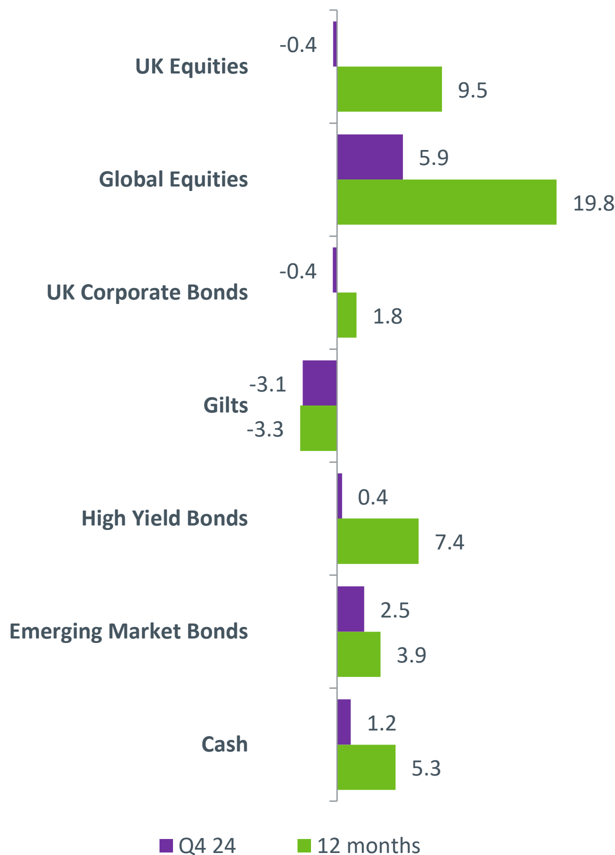
# Market Digest

## Q4 2024

### Monthly Highlights

- Trump's election victory drove strong performance of the US dollar and in the US equity market.
- The combination of Trump's election victory, comments from the Federal Reserve and the Chancellor's October budget helped push bond yields higher (bond prices fell).
- On page 3 of this document, we provide market commentary to cover the 12 months to 31 December 2024.

## Asset class returns (%)




*Source: Morningstar. Figures to 31 December 2024. Returns in sterling terms except high Yield bonds which are hedged. EM bonds are 50% local currency denominated and 50% US dollar denominated bonds.*

## Market summary

- Our model portfolios typically invest in a combination of the asset classes shown in the left-hand chart.
- The key market event over the quarter was Donald Trump's election victory. This drove strong global equity performance of almost 6% over the quarter.
- Even stronger performance was seen in the US market which gained 10% (in sterling terms) as Trump's policies, including tax cuts and deregulation, are seen as supportive for American stocks and the dollar.
- Other equity regions, especially those that look susceptible to US tariffs, such as Europe and Developed Asia-Pacific, underperformed.
- Despite the Federal Reserve (Fed) cutting interest rates twice over the quarter, the Fed signalled a slower pace of cuts moving forward into 2025. The Bank of England cut only once over the quarter.
- This signal of slower interest rate cuts, as well as the expectation of large government borrowing in the US and UK pushed up bond yields (bond prices fall as yields rise).
- At a portfolio level, equities tended to outperform bonds, resulting in higher risk portfolios producing greater returns than lower risk portfolios over the quarter.

## Outlook and topical market themes

- The Federal Reserve's "hawkish" cut persuaded investors that there will be fewer interest rate cuts in the US in 2025 than previously expected.
- UK GDP growth has halted over recent months, but should pick up again in 2025. At the same time inflation may continue to rise modestly over the next few months.

**Federal Reserve signals fewer interest rate cuts in 2025**

The Federal Reserve (Fed) had their final meeting of the year on 18th December. They chose to reduce interest rates by 0.25% to 4.25%-4.5%, as expected. What caught the market by surprise, however, was how much the Fed reduced the number of cuts that they forecast to make in the future. The last time the Fed had given their rate cut projections was September, when the median member expected 1% of rate cuts in 2025 and a cumulative 1.5% by the end of 2026. This is now a 0.5% cut over 2025 and 1% by the end of 2026.

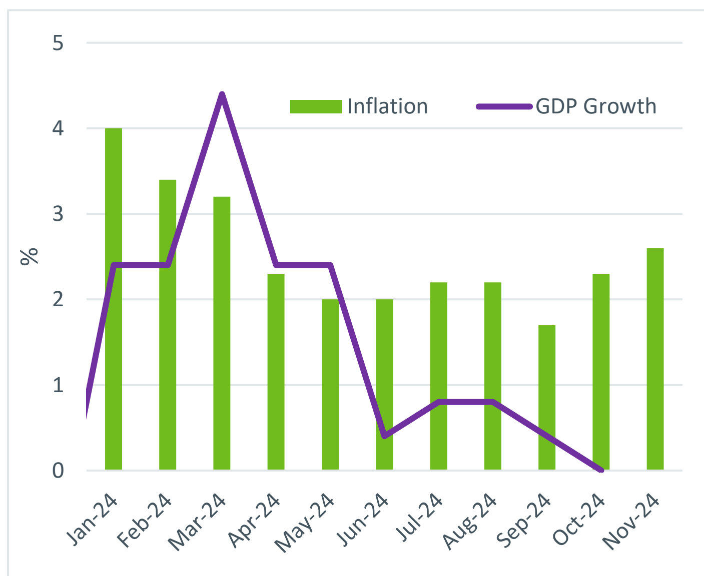
The market reaction was sharp as the US market fell almost 3% on the day (as the chart on the previous chart shows though, equity markets still posted strong performance over the quarter despite this drop) while bonds also fell as US Treasury yields rose 0.11%.

**UK growth is stalling, just as inflation is re-emerging**

Latest growth (GDP) data in the UK shows the economy stalled in Q3, with no growth recorded over the quarter. In addition, monthly data shows there has been cumulative growth of 0.0% between May and October 2024. At the same time, inflation has been rising from a low of 1.7% in September to 2.6% in November and is expected to rise further over the next few months. This 'stagflationary' environment is putting the Bank of England (BoE) between a rock and a hard place – hence their rather cautionary stance on cutting rates. As a result, yields on gilts (UK government bonds) have been rising rapidly since December, leading to concerns the government may be forced to increase borrowing further (or increase taxes/cut spending).

Things are certainly difficult for the BoE and the government, but there are some positive things to note. The Office for Budget Responsibility (OBR) expects the additional government spending, announced at the Budget, to boost growth in 2025. The extent of this is unclear, but it is reasonable to assume there will be some sort of government spending induced rebound. In addition, we don't expect a return to the level of inflation that we saw in 2022/23. A lot of the recent pickup in inflation is driven by changes to energy prices as well as volatile items such as plane and hotel prices. Underlying inflationary trends continue to fall, albeit slowly, so we could see CPI back up to around 3% later this year.

## Chart of the month – UK Economic growth has stalled as inflation starts to rise again




*Source: ONS. UK CPI inflation. 3m rolling annualised GDP*

The chart shows how economic growth stalled (purple line) over the summer and autumn in the UK. At the same time, the disinflationary process halted, and inflation (shown by red bars) even started to rise in Autumn.

We think the UK economy should start to grow again over 2025, especially as the increase in government spending starts to be felt.

Inflation may continue to rise further, but only to around 3%, before falling.

**Jack Richards**
**Investment Manager, HRIS**

## Annual market summary – covering the 12 months to 31 December 2024

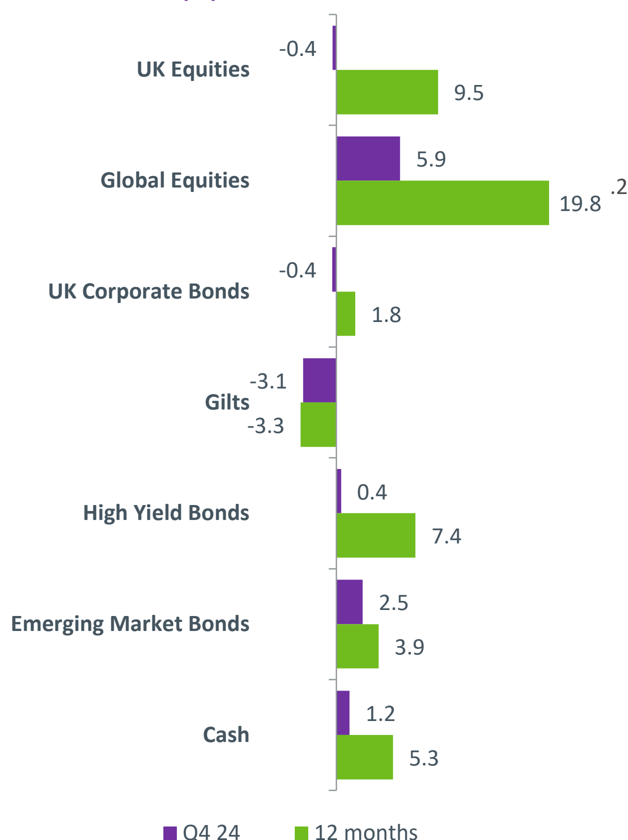
The key question for investors going into 2024 was how fast central banks would start to reduce interest rates. Of equal importance was what would be the reason for these cuts. Would it be because inflation had been contained or because of an economic slowdown? The answer, for now it seems, is the former. The Bank of England started cutting rates in August and has done so by 0.5% so far. The Federal Reserve (Fed) started later but has been cutting faster, by 1.0% in total. Economic growth, meanwhile, has held up, especially in the US.

Overall, the equity market had an incredibly strong year as the prospect of falling interest rates, without an economic slowdown, boosted investor sentiment. The strongest performance came from large American tech companies, especially chipmaker Nvidia, as enthusiasm towards leaders in the Artificial Intelligence (AI) sector continued. Even so, there were periods where anxieties towards an economic slowdown briefly appeared. In late August, a couple of weaker-than-expected data points temporarily caused panic around global markets. This spread to the Japanese market which fell by 12% in one day after a rapid strengthening of the yen. The panic was short-lived though, and the global equity market recovered in a matter of weeks.

2024 was dubbed as the year of the election, with over half the world going to the polls. The UK election had a limited impact on markets, given the strong expectation of a Labour victory going into election day. In the US, a close election was expected, but what we got was an emphatic victory for Trump. Markets quickly pivoted towards 'Trump trades' reflecting the expected winners and losers from Trump's expected policy agenda.

Bond performance was mixed over the period as expectations on inflation and interest rates were ever changing. Although central banks began their rate cutting cycle, bond yields ended up rising over the period. Trump's election victory was a big driver of bond yields upwards, as was the Budget in the UK. On top of that, strong US economic growth, and sticky inflation, lowered expectations as to how far central banks will cut rates. Given these events, gilts fell over the period, while corporate bonds managed to eke out small gains.

### Asset class returns (%)




*Source: Morningstar. Figures to 31 Dember 2024. Returns in sterling terms except High Yield Bonds which are hedged. EM bonds are 50% local currency denominated and 50% US dollar denominated bonds.*

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HYMANS ROBERTSON INVESTMENT SERVICES

London | Birmingham | Glasgow | Edinburgh

T 020 7082 6000 | hymansinvestmentservices.co.uk

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