2025 Market Outlook – Will the Trump TIGER roar?

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Trump 2.0 means a reset in US policy where tariffs will increase, taxes may be cut, the US will be more inward-focussed in terms of its foreign policy and in the control of immigration. In the near-term, growth-friendly policies are likely to support the economy, but it may also lead to a widening of the already growing US budget deficit.

Inflation is almost resolved, but 'almost' may not be good enough for market expectations about the pace of interest rate cuts in 2025 to be met.

With sticky core inflation and a slight pick up in headline inflation in the final months of 2024, central banks may be more cautious this year about how fast they cut rates. There will also be divergences this year among the pace of central bank cuts.

- The US Federal Reserve is likely to slow its pace of cuts probably more than the European Central Bank.
- Japan is likely to head in the opposite direction.

There may be surprises in store in currency markets as a result.

Growth in the US remained robust throughout 2024, with the latest data showing it accelerated[1]. Most forecasts suggest even if it does slow in 2025, fears of a US recession have receded. In the eurozone, where growth has been very slow, there are hopes that 2025 will see some recovery beginning. China appears to be stuttering to stimulate its economy and may continue to face headwinds.

Geopolitically 2025 is also likely to be a year of considerable change. With the prospect of the US playing a very different role in the Middle East and between Ukraine and Russia, the landscape may be about to change radically.

Earnings have also been a significant support to the gains made by investors over the past couple of years. The US equity market saw over 75% of companies in the leading US market index, the S&P 500, beat Q3 2024 company earnings expectations, while over half of the companies in the largest eurozone market index, the Stoxx 600, did the same[2]. A big part of this has been the exceptional growth[3] in the seven large technology companies, the Magnificent 7[4] as the artificial intelligence (AI) boom continued in 2024.

Rotations may also be a feature in 2025. The era of the outperformance of the Magnificent 7 hasn't ended but their dominance as a driver of market returns may be more modest in the years ahead. For our customers and investors this may mean having to think about other parts of the market, as other areas start to make up the gap.

A more normal era for bonds is to be expected where longer-dated bonds offer greater returns than short-dated bonds.

[1] Source: Bloomberg, 02.01.25.
[2] Source: LSEG I/B/E/S December 2024.
[3] Source: Bloomberg, 31.12.24.
[4] Alphabet, Amazon, Apple, Meta Platforms, Microsoft, NVIDIA, and Tesla.

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Outlook for 2025

Over the last two years, anyone invested in a diversified multi-asset portfolio has enjoyed exceptional gains but it seems unlikely that this pace of gains can be maintained into 2025.

However, a combination of a soft landing in the US economy and modest recovery in the eurozone, helped along by continuing interest rate cuts (even if more modest in the US), make for a combination that can support further (albeit) modest gains in risk assets, such as equities, as well as a more positive contribution from bonds. **But there are plenty of 'if's' behind this.**

- With a divergent path in interest policy emerging between the US, the eurozone and other leading countries, 2025 may be a year in which currency volatility is more prominent. With the US Dollar and Japanese Yen looking more likely candidates to strengthen in value.
- Over the last two years, equity markets have leaned heavily on the Magnificent 7 for returns and while these companies may continue to be world-beaters, their high valuations may weigh more heavily on future return outcomes. Other stocks likely to be positively impacted by the AI phenomenon, either in supply chain roles or directly in their business models, may be the next to feel the impact of this trend. It is likely the AI focus will remain on the US for now.
- Some investors may be attracted to high quality companies outside the US that have not yet been rewarded by the market. This could be more likely if the eurozone sees faster interest rate cuts and some economic recovery beginning.
- Bond markets should see the benefit of further interest rate cuts and a return to the norm of longer dated bonds earning more than their short-dated peers. There is likely to be a bumpy road in the months ahead, however, before inflation becomes more enduringly supportive.
- A soft US landing should also support high quality credit markets although it may slow down the returns from higher yielding riskier debt.

2025 Market Outlook Snapshot

- Unlikely the pace of strong market returns will be maintained.
- Central banks will show some caution this year in how fast they cut interest rates. Japan is likely to increase rates.
- Equity market returns reliance on the Magnificent 7 for returns may change, while these companies may continue to be world-beaters, the weight of their high valuations may impact future returns.
- Should the eurozone see faster interest rate cuts and some economic recovery beginning, high quality companies outside the US may start to see attractive returns.
- Bond markets should see the benefit of further interest rate cuts in 2025.
- A soft US landing should also support high quality credit markets.

As always, we encourage you to talk to an Advisor before making any change to your investment portfolio.

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