XPS Group

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Investment Briefing

Outlook for 2025: Trump 2.0 and 'Golden Ages'

Alasdair Gill, Partner at XPS Investment, recaps on 2024, the millennium to date, and outlines some pointers for investors for the next year.

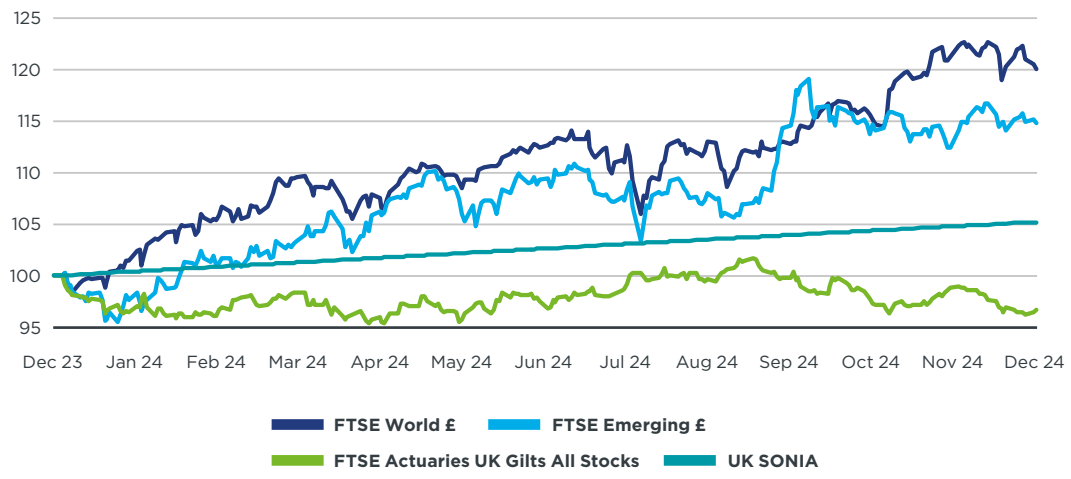
In 2024, politics took centre stage – will 2025 be a bit calmer in this regard? With President Donald Trump re-gaining the White House in the USA, alongside a supportive House of Representatives and Senate, this is unlikely! With the imposition of tariffs on China and the rest of the world likely, inevitable forays into geopolitics, and generally unpredictable announcements, we expect markets to be kept on their toes this year.

Deregulation and tax cuts could help mitigate some of the negative impacts of tariffs on the global economy, but there will certainly be winners and losers to evaluate in 2025. In this note we provide a recap on events in 2024 before reflecting on the last 25 years to see if any parallels can be drawn between the fate of technology stocks and address inflation then and now. We conclude with an outlook for 2025.

Recap of 2024

So back to 2024, which was another very strong year for equity markets, although it proved not so much for bonds. The chart here shows that global equities rose by 20%, again fuelled by the 'magnificent seven' although the rally was a bit broader than 2023. Bonds, by contrast, delivered a disappointing return, as the multiple rate cuts predicted at the start of the year stalled, and the path for rate cuts looks less clear as we head into 2025.

Chart 1: Asset Class Returns for 2024

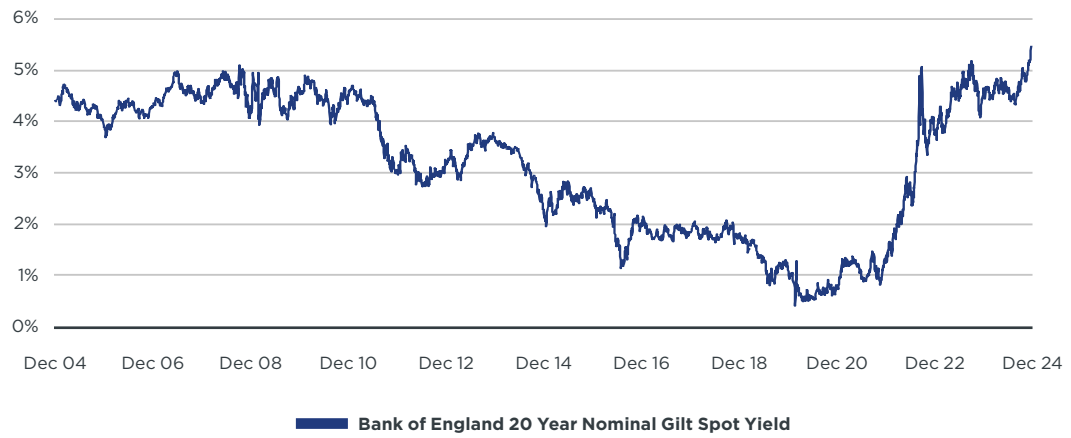


Source: Refinitiv

Bonds

Perhaps surprisingly, the yield on bonds continued to increase in UK and interest rate falls were not as material as expected in both US and UK during 2024. Hence yields are now truly back in the range last seen pre the global financial crisis and in many ways 'back to normal' for those with a longer time perspective (see later).

Chart 2: Bank of England 20 Year Nominal Gilt Spot Yield

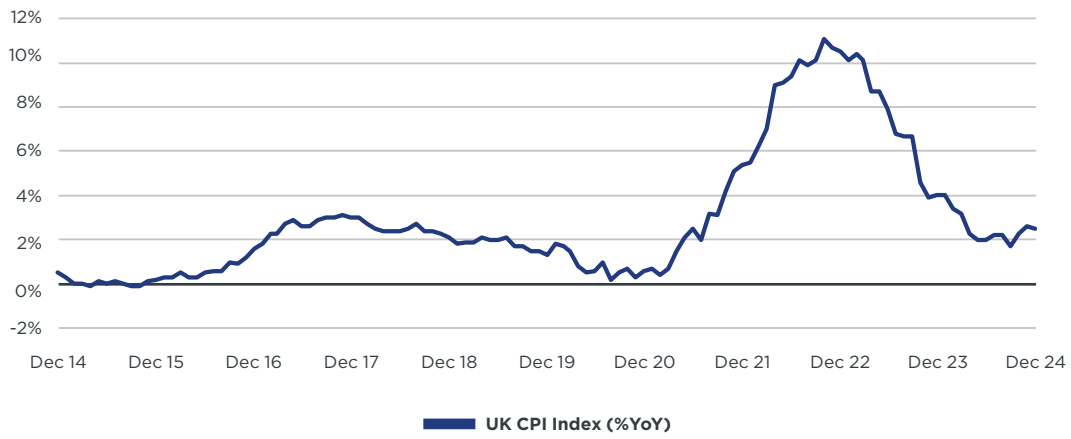


Source: Refinitiv

Inflation

Although inflation is back in the range that policy makers want, we could see signs that US inflation expectations may be turning higher (economy strong – corporate profits strong, consumer sentiment positive, employment remains resilient). In addition, many of Trump's policies such as tax cuts and tariffs could also be inflationary, and add to this upward pressure on prices. Hence, interest rates may stall at current levels rather than falling, as is still expected, although at a slower pace than was the case only a couple of months ago.

Chart 3: UK inflation to end December 2024



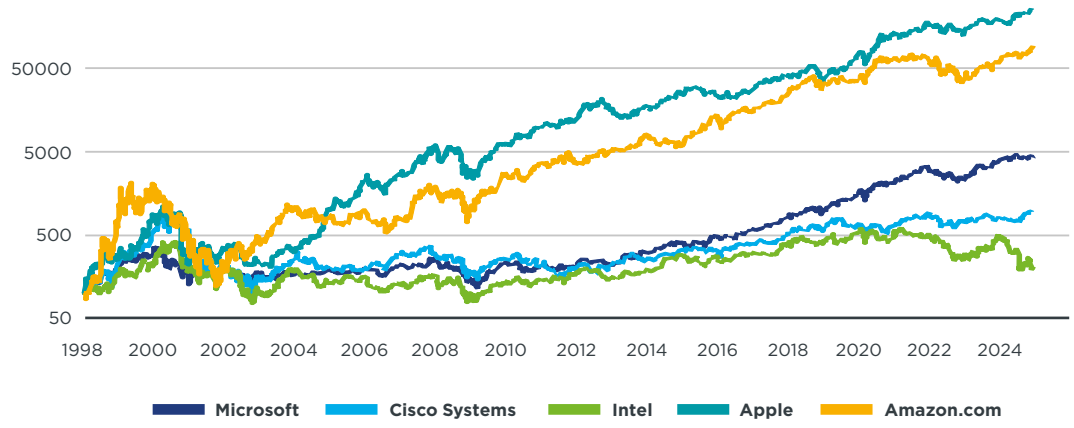
Source: ONS

A longer-term perspective – 25 years into the Millennium

Those of us who were working in the markets at the time of the Millennium were grappling with a couple of key issues. Firstly, there was a real concern that the 'Millennium Bug' would render many electronic gadgets (including computers) useless as they may not be able to compute dates post 1999 (which was largely unfounded). Secondly, there had been a concern about the Technology, Media and Telecoms (TMT) bubble: many stocks in these sectors had ballooned in value in the last two years of the Millennium, with new listings with flaky business models able to command huge valuations by listing, particularly on the Nasdaq exchange in New York. However, the music stopped in March 2000, with the realisation that many businesses were running out of cash and were worthless. Unlike the Millenium Bug this led to many months of market falls and the bankruptcy of many internet start-ups.

Stocks such as Amazon had ballooned by 1400% in 1998-99, only to fall back in 2000 by 80% (see chart 4). However, patient long term shareholders were eventually rewarded with a 18% per annum return in the following 25 years. Holders of Cisco Systems, however, were less fortunate – the stock was one of the darlings of the Millennium, becoming the Nvidia of its day – the stock however has never topped its $77 valuation at that point. Many smaller stocks disappeared from sight in the following months, but there were a few notable ultimate winners – Microsoft was actually the largest company globally in 2000, but also fell back by nearly 60% when the bubble burst, as they were the subject of various anti-trust law-suits. This great survivor has, however, still delivered – a solid 10% p.a. return, even since its highs in 1999 – indeed it is the only stock that was in the top 5 back then, and still up there now.

Chart 4: TMT Bubble survivors 25 years on (Log Scale)



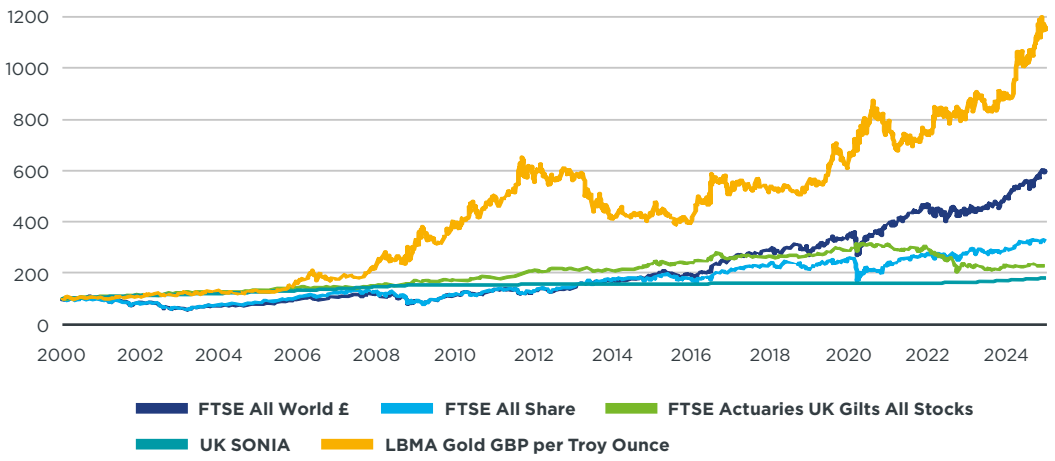
Source: Refinitiv

But what has been the best performing asset class of this millennium to date? Perhaps surprisingly, one of the oldest investments around, **Gold**, out-performed stocks, bonds and cash to deliver an impressive 10.3% p.a. return over this period[1]. This remains the case even if you move a year or two either side to reduce the impact of the TMT stock falls.

Whilst gold was a favourite diversifier in institutional portfolios in the early noughties, it did lose its lustre in the 2010s as a big fall of 30% in 2013 reminded investors of its potential for volatility, and led many to question its value in a portfolio as memories of the GFC faded, and new diversifying ideas emerged such as private credit, infrastructure, and crypto.

[1] Note that investors cannot achieve a return exactly in line with the gold price, as there are physical costs of storing the metal, etc. However, it is possible to invest in a gold backed fund such as an Exchange Traded Fund (ETF). The return on the longest running Gold ETF over 20 years has been 8.9% per annum, compared with a gold price rise of 9.2% p.a. over that period (both returns in dollars), showing that a return broadly in line with the gold price can be achieved.

Chart 5: Gold, Equities, Gilts and cash returns



Source: Refinitiv, World Gold Council

What does this tell us about the outlook for 2025 and beyond? Having sustained such a rally it does feel like gold looks relatively expensive, and it is arguable how useful this (or indeed other commodities) asset class can be as a diversifier, although there is no doubt that it does tend to do well in a severe downturn. There are some similarities to their new cousins, crypto assets (not available 25 years ago) although crypto has tended to be too correlated to risk assets (whereas gold has typically shown low or negative correlation). See my colleague Simeon Willis' **paper** on crypto for XPS's views on that asset class.

Looking ahead

As in previous years, we outline our view on the main asset classes for 2025 and beyond, beginning with equities.

Equities

Last year we expected the equity bull market to broaden out – although it did to an extent, the dominance of the larger tech sector persisted. This year, we do expect that there remains scope for global equities to deliver positive (but more muted) returns, and unlike 25 years ago, the large tech stocks are generally delivering increasing profits to justify their pretty full valuations (when looking at metrics such as price/earnings to growth). However, with President Trump's unpredictability in the background, this could hit sentiment and lead to market volatility, particularly in the US and China. However, his more positive noises on tax cuts could boost earnings among more domestically focused smaller and mid cap companies.

The UK domestic market looks decent value, and although the new government has yet to demonstrate how they will stimulate growth, there is scope for some re-rating of stocks, particularly those with a global reach.

In emerging markets, although returns have been improving, valuations remain relatively attractive. However, we would still urge caution as China will be particularly susceptible to Trump tariffs hitting exports, and this economy continues to exhibit structural challenges, with ongoing property market issues, and stubbornly high savings ratios which has resulted in weak domestic demand.

Overall, conditions are in place for another decent return for equities this year, perhaps high single digits, with a bit of volatility along the way.

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Bonds

Chart 6: Additional Yield on Corporate Bonds



Source: Refinitiv

As per chart 2, bonds now offer a better yield in excess of inflation to investors, and although the additional yield on corporate bonds is relatively low compared to its history (chart 6), overall yield levels are supportive for income hungry investors. We therefore believe that high quality bonds have a larger claim for space in multi-asset portfolios than higher yielding issues, which offer a limited additional yield for the additional risk taken on. So for bonds we would expect a yield driven return for high quality bonds, with relatively stable capital values, and limited or no additional returns for higher yielding issues.

What about alternatives?

Property yields continue to rise despite vacancy rates rising, and so there remains scope for further income growth if vacancy rates fall. We are also seeing an easing of some of the headwinds in the sector over the last 12 months, with even prime offices starting to pick up as more businesses are asking staff to be more present in the office. Other alternatives such as infrastructure we see as more of a 'buy and hold' type investments, which should tick along although it can be difficult to get capital deployed.

And finally, what of gold? Given its incredible run, it is difficult to be too 'bullish over bullion' from here, and it remains arguable as to whether it functions well as a diversifier – longer term investors can do better using assets with more visible return drivers, although gold can provide a hedge against 'unknown unknowns'.

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Summary

Overall, we expect that President Donald Trump will keep everyone guessing with his aggressive interventions, but we still expect economic growth to emerge and support a positive year for markets. We do not see a parallel with the 'dot com' boom and bust of 1999/2000, as the key businesses driving the markets this time round are actually profitable!

As ever, however, there remain many risks to the downside, and although politics could be a bit calmer, we do continue to have the potential for geo-political risks to introduce volatility and periods of turbulence.

Hence it is important for growth investors to maintain a diversified portfolio, which should include assets such as bonds which now have a more supportive yield, and other diversifiers – but perhaps not our old friend gold.

Find out more

For further information, please get in touch with **Alasdair Gill** or speak to your usual XPS contact.



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