December 2024

MONTHLY HOUSE VIEWS

2025 OUTLOOK

Macro

Citi's global economic surprise index turned lower in late November on disappointing PMI business confidence surveys and ended the month marginally in negative territory. However, this had no impact on consensus global GDP growth for this year and next which remain at 3.1%, the high for the year. Nonetheless, this remains a two-speed economy – activity in global manufacturing is contracting as companies recalibrate their supply chains while business confidence in services remains robust. Sentiment in services has been bolstered by generally low unemployment rates, accommodative fiscal policies and abundant liquidity, which has pushed global stock markets to all-time highs, reinforcing the "wealth effect" for consumers of services. In terms of regions, the US continues to lead other major economies while China has still to reap the rewards of its recent policy easing and Europe remains stuck in the doldrums.

Central Banks

The US Federal Reserve (Fed) cut rates last month by -25bp as was widely expected, and chairman Jerome Powell reaffirmed the central bank's independence by stating he would remain in his position even if asked to leave by newly elected President Trump. In the course of the month, there was a notable improvement in animal spirits as business owners and investors savoured the prospect that tax cuts and deregulation might kickstart an economic recovery. This raised worries that inflation might not subside back to target as quickly as hoped and traders correspondingly revised the number of expected -25bp rate cuts before the end of next year from four to three. In Europe, there was little change in the consensus expectation that the European Central Bank (ECB) would cut rates by -25bp.

Markets

The MSCI World index of global equities jumped 4.5% in November, the eleventh monthly gain since the rally began in late October 2023. Much of last month's strength could be attributed to the 5.7% post-election rally in US equities, while Japan edged 1.2% higher and Europe shed -1.8% in dollar terms. The strength in global equities was broad-based with only Materials and Health Care losing ground in November. Among factors, Growth led the way with a 5.3% bounce, closely followed by Momentum and Value which added 4.1% and 3.7% respectively. Bond markets stabilised after October's -3.4% drop, advancing 0.3% over the course of November. In currency markets, the dollar continued October's rally with a 1.7% gain in November on post-election euphoria.

Bottom Line

We have kept our recommended equity allocations unchanged at modestly Overweight and we continue to balance exposure to the major US technology and internet platform stocks with positions in mid-cap equities. For now, we continue to favour US stocks over Europe and Asia. In terms of factors, we call for keeping a balance between Growth and Value stocks. Our allocation to US duration (i.e., sensitivity to changes in rates) remains at Neutral, while credit spreads (the difference in yield between corporate and sovereign bonds) have tightened further – we suggest bond investors remain very selective.

Summary House Views

OUR ASSET ALLOCATION

The tables below present the latest conclusions of our Global Investment Committee.

Equities	Equity performance has pushed allocations into Overweight territory. We continue to recommend investors strike a balance between Value and Growth. We prefer the US to Europe and Asia.	Overweight
United States	We have adjusted our US allocation to achieve a better balance between Growth and Value. Quality and Growth stocks have dominated this year's market performance, but their valuations are getting stretched.	Overweight
Eurozone	The bear story for Eurozone equity markets is well-known. However, the markets are still cheap, still under-owned and still in an uptrend.	Neutral
UK	Recent macro data in the UK has shown some improvement, and the equity market has begun to catch up with its neighbours.	Neutral
Switzerland	The Swiss market is dominated by high-quality, defensive stocks, which should help cushion any downside, while inflationary pressures remain well below those suffered by its neighbours.	Neutral
Japan	Recent volatility in the yen against the US dollar could encourage investors to reassess the outlook for Japanese stocks which could in turn interrupt their bull run for now.	Neutral
Emerging (EM)	The Chinese authorities have taken some measures to shore up domestic equity markets and Chinese stocks look cheap in light of expected earnings growth.	Neutral

Fixed Income	Sticky inflation readings and fears that President Trump's policy could prove reflationary have pushed bonds back into negative territory for the year to date. We continue to prefer equities.	Underweight
Sovereigns	As bonds have rallied, the yield curve normalised, and 10-year yields have moved back above 2-year rates. Any signs of sticky inflation combined with weak macro could accelerate this move.	Underweight
Duration	We have now rebuilt a Neutral allocation in duration which has both reduced our Underweight compared to the market and provided a hedge against macro weakness and Fed easing.	Neutral
Inflation-linked	Inflation-protected securities tend to have very high duration, making then extremely sensitive to small shifts in inflation expectations.	Neutral
Investment Grade	Elevated policy rates and inverted yield curve have created some buying opportunities in short-dated high-quality corporate bonds. We remain Underweight nonetheless.	Underweight
High Yield	Credit spreads have tightened to unattractive levels, especially if growth weakens. Investors should remain highly selective given the potential for a deterioration in credit quality.	Underweight
Emerging debt (in € and $)	In recent months, we have warned that political risk in Latin America required careful monitoring. The reaction to June's presidential elections in Mexico underlined this point.	Neutral

↗ Upgrade ↘ Downgrade ⊕ Overweight ⊜ Neutral ⊖ Underweight

Commodities	Although the long-awaited recovery in China will eventually boost demand for raw materials, worries about a slowdown in advanced economies next year lead us to keep allocations to commodities at Neutral.	=
Energy	With OPEC+ cutting output and oil majors reluctant to invest in new production capacity, crude oil supply is constrained. However, fears of economic slowdown in the west have kept prices rangebound.	=
Industrial metals	The key driver for industrial metal prices will be Chinese demand once the economy finally picks up. We also continue to highlight the attractions of transition metals like copper.	=
Precious metals	Central bank demand for gold remains strong and bullion continues to provide useful diversification benefits in terms of portfolio construction.	+

Currencies	The dollar index remains stuck in the wide trading range which has been in place since late 2022. Donald Trump's clear election victory helped the index rally 1.7% last month towards the top of its range.	
EUR/USD	The euro's rally from its April lows against the dollar appears to have reversed now that the Federal Reserve has commenced its rate cut cycle.	=
GBP/USD	The UK's growth outlook has begun to improve despite its structural weaknesses, and the strong majority won by Labour means the country faces little political uncertainty over the next few years.	=
EUR/GBP	Both currencies face numerous challenges, but the lack of political uncertainty in the UK and the country's improved economic performance have pushed sterling higher.	=
USD/JPY	Global investors began to unwind some of their "yen carry trades" (constructed by borrowing in yen to invest in higher-yielding assets in foreign currencies), but there has been renewed dollar buying recently.	=
EUR/CHF	After weakening sharply from January to late May, the Swiss Franc commenced a rally which has taken it back to January's levels, despite the likelihood of further SNB rate cuts.	=
Emerging	EM currencies have tracked generally lower against the US dollar in recent months, reaching new all-time lows, and have yet to show any sign of building a base.	=

↗ Upgrade ↘ Downgrade + Overweight = Neutral − Underweight

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Economic Outlook

FED – BETWEEN TWO ROCKS & A HARD PLACE

Over the past few weeks, strategists at Wall Street banks, institutional asset managers and private banks have been busy publishing their 2025 outlook reports, which have been generally upbeat on the economy and bullish on risk assets, especially US equities. This stands in stark contrast to their forecasts twelve months ago when US recession fears dominated, a pessimism that proved unfounded as the economy has reaccelerated towards 2.7% GDP growth and US equities have recorded their second consecutive year of over 20% returns. Will the US economy confound consensus expectations yet again? And what might that mean for financial markets?

The US job market data for November painted a mixed picture. The increase in non-farm payrolls in the establishment survey bounced back from October's hurricane-and-Boeing-hit low, jumping from 36'000 new jobs to 227'000. Although November's figure was well above the average of 201'000 for the twelve months to September, the October-November average of only 131'500 does not suggest a reacceleration in job growth.

Similar mixed signals were to be found in the parallel household survey. Despite the jump in non-farm payrolls, the unemployment rate ticked up to 4.2% in November. It has been rising steadily since April last year, up 1.7 percentage points since then. And unlike the establishment survey, households reported a -723'000 drop in the number of people in employment in October and November. In addition, the number not in the labour force rose to 101.2 million, the highest level ever outside of the pandemic-era lockdowns. Moreover, the number of long-term unemployed continues to rise. There are now 1.7 million Americans who have been out of work for 27 weeks or longer, a 42% rise from this time last year and the highest level in almost three years.

In recent decades, the Fed's independence from political influence has been largely unchallenged. The singular exception to the independence norm came during Donald Trump's first presidency when he used his Twitter pulpit to criticise Fed policymakers on more than one hundred occasions according to the Brookings Institute. Much of the criticism came after Trump had appointed Jerome Powell as Fed chairman, believing him to be a "low-interest rate guy", only to see him keep rates well above those of trade partners like the Eurozone. This prompted the President to declare that Powell was a "bigger enemy" than Chinese President Xi Jinping.

During his 2024 presidential run, President-elect Trump sent clear signals that the pressure would resume once he was back in the White House. On August 8th for example, he declared that he believed he should "have a say" in setting monetary policy. Since then, he has sounded more emollient, declaring recently that he would not seek to oust Powell before his term expires in May 2026. However, this would not preclude renewed strong criticism from the White House in the interim. Moreover, some aspects of Trump's policy platform could make life difficult for Powell – most notably, his promise to impose swingeing tariffs on imports could push inflation back above 3.0% according to Goldman Sachs.

The job market and Trump pressure both suggest an easing bias to monetary policy.

The market reacted well to the recent US consumer price inflation (CPI) figures. The probability of a -25bp rate cut in December jumped from 86% to 98% as traders took comfort from the fact that price rises came in line with expectations and judged that the Fed could continue to ease policy.

The November headline CPI rose 0.3% month-on-month (MoM), the fastest pace since April, while the year-on-year (YoY) rate hit 2.7%, up from 2.6% in October. These increases came despite the shelter component slowing to 0.3% MoM from 0.4%, as many traders had been hoping. And services and goods prices were both up 0.3% MoM, the same pace as October However, there were accelerations elsewhere – for example, food prices rose 0.4% MoM versus 0.2% the previous month. At the core level (which excludes volatile food and energy prices), the CPI rose 0.3% MoM and 3.3% YoY, both unchanged from October.

If we look at the annualised trend in inflation over recent months, the reacceleration becomes clearer. Core CPI appears to have turned higher. The annualised rate over the past six months hit 2.9% in November, up from 2.6% the two previous months, while the annualised three-month rate has shot up from 1.6% in July to 3.7% last month.

This tendency is corroborated by other measures – for example, although the Atlanta Fed's index of twelve-month Core Sticky CPI has been slowing, it was still at 3.9% in November. Moreover, producer prices are on the rise again. The producer price index (PPI) hit 0.4% MoM and 3.0% YoY for November, well above expectations for 0.2% and 2.6% as well as October's 0.3% and 2.6%.

In this context, we are sceptical that the Fed will feel comfortable with bullish market expectations for rate cuts next year. We would not be surprised if the tone of policymakers' statements does not turn somewhat hawkish after December's rate cut.

Bottom Line

Next year, the Fed is likely to find itself in a bind. On one hand, the twin "rocks" of a weakening labour market and relentless pressure from President Trump could push chairman Powell to accelerate rate cuts. On the other, the "hard place" of persistent, sticky inflationary pressures could severely limit the Fed's scope to ease policy. The clash between these opposing dynamics could well challenge the consensus optimism for 2025.

EQUITIES

The MSCI World index of global equities rallied to end November up 4.5%, taking year-to-date returns to 20.2%. The strength was broad-based across factors – Growth, Quality, Value, High Dividend Yield and Momentum all rose between 1.8% and 5.3%. After underperforming in July and August, the very largest global companies remained at the top of the leaderboard for the third straight month – the Magnificent Seven index of the biggest US tech and internet platform companies soared 9.4% in November. Smaller companies also did well last month – the MSCI World Small Cap index jumped 6.4% last month. At the regional level, Europe underperformed the US sharply yet again (-1.8% versus 6.1% on the MSCI indices) while emerging markets dropped -3.7% over the month (all data in dollar terms).

US . After dropping sharply from 85% to 48% over the course of October, the proportion of US stocks trading above their 50-day moving average (DMA) jumped back to 71% last month. In terms of factors, the strength was broad-based – Growth led the pack with a 7.0% rally while Quality brought up the rear with a decent 4.3% gain. At the sector level, Consumer Discretionary and Financials both jumped by over 10% while Health Care only managed to edge 0.1% higher, continuing recent underperformance on fears that the incoming Trump administration could clamp down on healthcare spending. The equal-weighted version of the S&P500 slightly outperformed its market-cap-weighted sibling in November, up 6.2% versus 5.7 %. And smaller companies outperformed for the first time in four months – the S&P Small Cap 600 index soared 10.8% last month.

The rally in stocks since October 2023 has pushed S&P 500 valuations up from 19.1x trailing earnings to 25.3x. At these levels, hopes are high that analysts' optimism will prove well-founded. Currently, they expect S&P500 index earnings to grow by 13.2% over the next twelve months according to Bloomberg, which is substantially above the final results for Q3 – earnings-per-share were up 8.5% year-on-year. This has pushed the trailing valuation premium over European stocks to 11.2 points on MSCI data, well above last October's 7.9 points. This premium cannot fully be explained by the market-dominant valuations of the Magnificent Seven stocks – the valuation premium of US IT stocks over their European peers is one of the lowest among sectors at 24.8%, well below consumer discretionary and financial stocks, which are 133.4% and 104.4% more expensive respectively. The same holds true for factor indices – according to MSCI, US Growth stocks trade at a 59.3% premium to Europe and US Value 82.2% higher. We continue to call for a blend of Growth and Value stocks in portfolios.

Europe . The accumulated effect of negative economic, political and geopolitical newsflow has made it easy to be bearish on European equity markets in recent years. The macro backdrop is indeed worrisome – business confidence in manufacturing has been stuck in contraction territory since July 2022 and the real economy has only grown at an annualised 0.3% rate over the past seven quarters. On the political front, both the German and French governments look set to fall in coming weeks, which could leave the European Union rudderless in the run-up to President Trump's inauguration on January 20th. The geopolitical backdrop also remains problematic – the war in Ukraine continues to drag, which has fragilized Europe's energy supplies, the near-East conflict between Israel and Iran's proxies in Gaza and Lebanon will exacerbate Europe's refugee crisis, while Houthi attacks on cargo ships in the Red Sea continue to disrupt supply chains, adding to inflationary pressures on the key Asia-Europe freight route. In addition, investors continue to shy away from European equity funds – according to EPFR, redemptions since the start of this year now total -$61.2bn. Nonetheless, European equity markets continue to offer decent performance, despite recent sharp weakness – since October 2022, the EUROSTOXX index has provided a net total return of 33.4% versus 49.1% for the S&P 500 in euros.

In valuation terms, European equities continue to look cheap compared to history and to other markets, notably the US. As highlighted above, the MSCI Europe index trades at 14.3x trailing earnings versus 25.5x for its US counterpart. Moreover, European stocks are expected to pay investors a handsome 3.6% dividend yield in 2025, almost three times the forecast 1.3% yield on the MSCI US index.

Emerging Markets . There was broad-based weakness in emerging market regions again last month –Latin America and Asia tumbled -5.7% and -3.7% respectively while Eastern Europe outperformed slightly with a -0.6% drop. Within countries however, there was great divergence. Argentina actually skyrocketed 19.7% in November, on the back of President Milei's success in bringing the monthly inflation rate down from 25.5% last December to 2.4% in November. At the other end of the spectrum, Indonesia tumbled -6.9% while South Korea fell -5.2% (all data in dollar terms).

Factors . Growth stocks outperformed Value for the third straight month according to MSCI's factor indices. As is to be expected, earnings forecasts for Value are modest – the consensus expects only 3.6% growth over the next twelve months versus 14.5% for Growth. But this is reflected in valuations – global Value stocks trade at 15.5x trailing earnings versus 32.3x for Growth.

Bottom Line

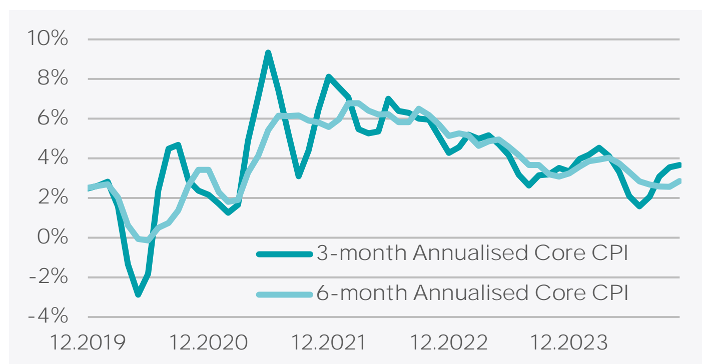
Our Investment Committee has decided to keep equity allocations unchanged for now, at a modestly Overweight allocation to stock markets. Our geographic preferences remain unchanged, with the US preferred to Europe and Asia. The discrepancy between Value and Growth has become extreme and we reaffirm our suggestion to take some profits in megacap technology stocks and to add to holdings in small and mid-caps.

FIXED INCOME

Bloomberg's Global Aggregate bond index edged 0.3% higher in November, its sixth advance in the last seven months, leaving the up 0.5% for the year so far. This leaves the pattern of higher highs and higher lows which commenced in October 2022 unbroken.

US . The main event of November was undoubtedly Donald Trump's election to the White House and the accompanying Republican sweep of Congress. This sparked a rally in the stock market on optimism fuelled by the prospect of deregulation and a more pro-business government. The dollar also rose on expectations that the US's main trading partners might let their currencies weaken to mitigate the impact of Trump's promised tariffs imposed on imports, in particular from China. Bond yields were also up on the fear that his policy platform would prove inflationary, although the appointment of Scott Bessent, a fund manager, as Treasury Secretary did calm the bond market as he is viewed as a source of stability in the administration.

The markets are currently very optimistic, which has boosted asset prices – a pullback is increasingly likely, although its timing is uncertain. In the United States, growth is steady around 3% and there does not appear to be an imminent catalyst for a significant slowdown, financial conditions are easy, and the Fed seems inclined to continue cutting rates, which should continue to support asset prices. One potential trigger for a pullback could be over-indebtedness – but the private sector has been deleveraging for some time, which only leaves the government as a source of excessive borrowing. However, this has long been the case and, until something triggers stress in the Treasury market, there should be little impact on growth.



Source: Bloomberg

We expect short-term interest rates to continue to decline in the US, but at a slower pace. The three-month annualised change in CPI and Core CPI has started to move higher (see chart above) and, with credit spreads close to their tightest levels and stock markets making new highs, it is very difficult to argue that financial conditions are too tight. Part of the new administration's economic plan is to increase oil production by 3 million barrels per day, which would surely have a positive impact on inflation, but such an increase would take years to implement.

Europe . In Europe, it is a different story as there are clear challenges to growth. Core inflation remains high across the Eurozone. However, a resolution in the Ukraine conflict, which President-elect Trump has promised to negotiate early in his term, could mean sanctions being lifted which could ease Europe's energy crisis and lower prices of Russian imports. We expect rates cuts to continue at a moderate pace in the Eurozone.

In Europe, lower growth is already reflected in the very low yields. I am also cautious on highly indebted countries such as France given the risk of a debt crisis like the one that took place in the UK in 2022. Back then, the Bank of England was forced to intervene when Liz Truss's short-lived government attempted to push through unfunded tax cuts. More recently, France, which is experiencing a toxic combination of political uncertainty and out-of-control government spending, has seen borrowing costs rise above Spain's and close to Greece's – French ten-year yields ended October at 2.89% versus 2.79% for Spain and 2.91% for Greece.

Credit . We remain constructive but selective on credit in general. As discussed in previous letters, the reward for taking credit risk is very low with high yield spreads reaching the tightest levels since 2007. However, the private sector has been deleveraging which has improved balance sheets in general. This deleveraging was reinforced after the last hiking cycle in 2022 when over-leveraged companies were forced to restructure their balance sheets. Indeed, some of the companies that were in trouble back then are now able to refinance debt at more attractive levels. For example, a Swedish real estate developer was able to issue a perpetual bond at 6.25% in November. The yield on the company's previous perpetual was higher than 12% at the peak in 2023. This is a clear sign of easing of financial conditions.

Bottom Line

Although we remain defensive overall in our fixed income allocations, with a clear focus on high quality credit, we have now rebuilt a Neutral allocation in duration given the risk that we could see some economic weakness in coming months.

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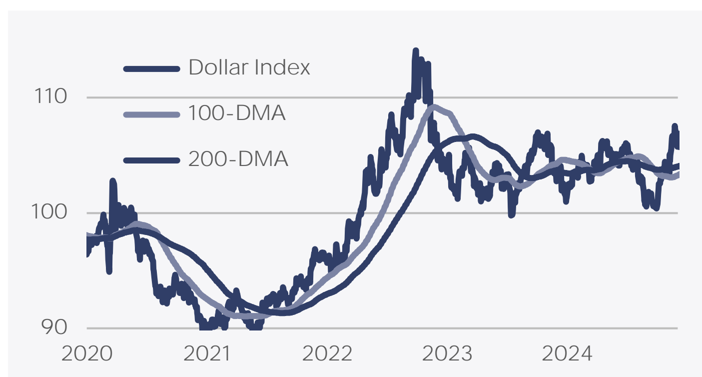
CURRENCIES

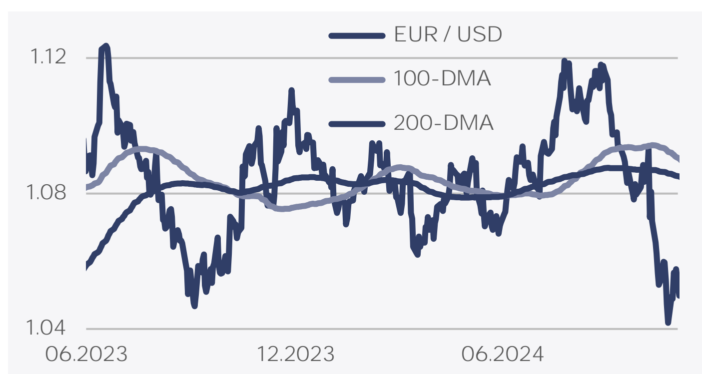
Since late 2022, the dollar index has been stuck in wide trading range between 100 and 107 points. Donald Trump's clear election victory and business-friendly stance helped the index rally 1.7% last month towards the top of its range.

USD . The election of Donald Trump was a clear positive for the dollar. The threat of tariffs set off selling pressure which weakened the currencies of the US's main trading partners. As mentioned on page 6, we also expect the spread between American and European short-term rates to increase, which would weigh on the euro.



Source: Bloomberg

EUR . This being said, we would caution against shorting the euro or European assets at the moment given the pervasive pessimism on the region (see page 5). Any incrementally good news for the Eurozone could lead to short-covering and portfolio rebalancing in favour of the Europe. Positioning against the euro is currently extreme – short positions recently hit a four-year high, which suggests that a counter-trend rally could last several months. As a reminder, the dollar recorded a strong rally between Trump's election victors in 2016 and his first weeks in the White House, only to reverse course and fall -12.4% against the euro over the course of 2017. Back then, Macron's election in spring 2017 contributed to renewed optimism on the Eurozone. In the coming months, the positive surprises could come from a shift in German fiscal policy after the forthcoming elections as well as possible peace talks between Ukraine and Russia.



Source: Bloomberg

COMMODITIES

Global spot commodity prices rose 0.3% in November, their second straight advance, pulled higher by rising agricultural prices which offset weakness elsewhere.

Energy . November was an uneventful month for crude oil prices as traders awaited the scheduled OPEC+ meeting on December 5th. Brent and WTI traded in a tight trading range over the month, the narrowest since May. On one side, geopolitical tensions remain high, especially in the Persian Gulf and with Russia, maintaining fears of supply disruptions. Moreover, there are persistent rumours that OPEC+ might extend its output cuts beyond its end-2024 deadline in an attempt to put a floor under crude prices. On the other, sluggish growth in Europe and China means slower growth in demand for oil. Moreover, Donald Trump has been returned to the White House amid calls to "drill, baby, drill" and promises from Scott Bessent, his pick for Treasury Secretary, to increase US crude production by 3.0 million barrels per day (mb/d). This is a big deal – the US is already the world's largest oil producer, output there recently hit 13.5mb/d, its all-time high, and such an increase is equivalent to around 2.9% of global demand. At the same time, OPEC+ is already withholding some 5.9mb/d of production according to Reuters, representing another 5.7% of global demand. The risk of a supply glut is growing.

In its November report, the International Energy Agency (IEA) forecasts that oil demand will expand by 0.9mb/d this year and 1.0mb/d next, taking global demand to 102.8mb/d and 103.8mb/d respectively. It attributes this sluggishness to the end of the post-pandemic bounce in demand, weakening global activity levels as well as the inroads made by alternative energy sources. The IEA also noted that non-OPEC+ producers, led by the US, will add 1.5mb/d this year and next, leaving the market with a structural overhang of supply over demand.

Gold . Gold prices fell -3.7% in November, after hitting its all-time high at $2'788 per ounce in late October, taking year-to-date performance to 28.1%, the best in over a decade. Central banks, notably in developing markets, have emerged as a significant source of demand as they seek to diversify their foreign exchange reserves away from G7 currencies. After a pause in buying in August, purchases resumed in October with 47 tonnes (t) added to reserves, the largest purchases year-to-date. The most active buyers in October were Turkey, Poland and India, as has been the case since the start of the year. Their central banks have each bought more than 60t so far this year and together represent over 70% of total central bank purchases over the period. After six months of steady inflows into gold exchange-traded funds (ETFs), November saw the equivalent of -29t of redemptions, which flipped aggregate trading in gold ETFs since the start of the year to net sales of -11t. However, the strength in gold prices means that assets under management in gold ETFs ended November at $274bn, up around 26.5% year-to-date.

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