MONTHLY INVESTMENT REVIEW

February 2025

VINTAGE ASSET MANAGEMENT

Market returns were mostly positive in January, when the likely extent of trade wars and the arrival of a new player in the artificial intelligence or AI market had a particular impact. There was variable news on the previously encouraging factors on inflation, interest rates and economic growth while company earnings as well as corporate activity proved largely supportive.

Donald Trump's inauguration as America's 47th president saw a flurry of executive orders including the declaration of an emergency on the border with Mexico, the US withdrawals from the Paris climate accord and the World Health Organisation and the ending of all the government's diversity, equity and inclusion programmes - large companies such as Meta also curtailed their previous commitments. The president declared an energy emergency and ended the requirement for half of new cars to be electric. While the administration terminated funding for renewable energy infrastructure introduced by its predecessor it announced a new project to fund spending in AI, which was met with some disdain by Elon Musk.

US shares were hit by a sharp sell-off over the threat to the established order in AI from a Chinese rival DeepSeek with its lower cost and open source approach. The value of large technology shares dropped by $1trn on 27th January, more than half of that represented by Nvidia which saw a 17% fall in its share price, if only to levels last seen in September; Broadcom fared even worse. European markets fared well in the month given their relative value in spite of the challenges; the prospect of an end to the war in Ukraine, if with higher defence spending, helped as did a potential boost to the German economy from a less rigorous restriction on government debt, if dependent on elections.

The likely trade issues from the Trump administration have tempered expectations and added to the potential volatility. While markets initially took comfort from the lack of specific proposals they now need to assess the imposition of tariffs of 25% on Canada and Mexico as well as the 10% on China, while the US president has the European Union and perhaps the UK in his sights. Trading partners will retaliate. US traders amassed gold on the basis that it might face new duties.

The Bank of Japan raised interest rates from 0.25% to 0.5%, the third increase since it ended its policy of negative rates last March; the prior rise had been as far back as July and the Bank's governor, Ueda Kazuo, revised upwards its inflation forecast while pointing to further rate rises. The US Federal Reserve opted to hold its interest rate in the range of 4.25-4.5% in spite of pressure from the new president to reduce it; the market expectation is of a further cut of a quarter of a percentage point by the summer although the Fed's committee meeting minutes were non-committal. The Bank of England is expected to cut its rate again this month from the current 4.75%, even as inflation stays above 2% in part as the economy barely grew at the end of 2024.

The European Central Bank (ECB) again reduced its interest rate on deposits, from 3% to 2.75% following the four cuts in 2024, in part as it too was concerned over the weakening economic outlook.

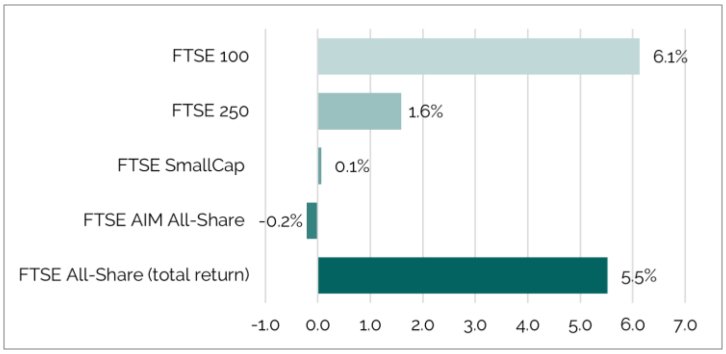
The rate of inflation has remained variable and much has depended on the pattern a year earlier in the developed economies. In the US the consumer price index (CPI) rose once again to 2.9% in December from 2.7% in November although the core rate excluding fuel and food was down from 3.3% to 3.2%. Tariff wars are likely to have an inflationary effect over time. In the UK the CPI was unexpectedly down to 2.5% in December from 2.6% for November. In the eurozone the rate of consumer price inflation was up from 2.2% in November to 2.4% in December.

The US economy grew at a lower rate than expected at 2.3% in the last quarter of 2024, down from 3.1% in the third quarter; personal consumption remained the main driver of growth, rising by 4.2% which was up from 3.7% in the prior period and the highest rate since the first quarter of 2023 although fixed investment contracted for the first time since then. The eurozone economy expanded by a reported 0.9% in the fourth quarter, held back by France which saw a decline of 0.1% and by Germany which was 0.2% weaker; the data confirmed that the German economy had contracted by 0.3% in 2024 after a decline of 0.3% in 2023, with weakness in manufacturing and construction. In the UK the government looked again to boost a sluggish economy while seeing its fiscal flexibility fade.

The various political or geopolitical considerations persisted or developed. Ahead of the German elections on 23rd February there was controversy as Friedrich Merz of the Christian Democratic Union sought the help of the far-right Alternative for Germany (AfD) to pass measures to restrict migration. A ceasefire held between Israel and Hamas in the Middle East. Mark Carney stood for leader of the unpopular Liberal Party in Canada. The political problems persisted in South Korea where the president Yoon Suk Yeol surrendered to the authorities and faced more charges over his brief introduction of martial law in December. The tension over Taiwan simmered, and the war in Ukraine dragged on, with Russia making territorial gains ahead of likely peace talks as the Trump administration threatened crippling sanctions. The conflict in the Democratic Republic of Congo escalated.

Corporate earnings have been robust if varying by sectors. JPMorgan saw profits increase by half to $14bn in the last quarter of 2024. Questions over the benefits of the heavy investment on AI led to a fresh assessment of valuations, against a backdrop of higher bond yields which moderated a little. EY reported that one in five UK quoted companies had issued a profit warning in 2024, the highest ratio for twenty-five years. Corporate activity remained robust with deregulation and low taxes in the US.

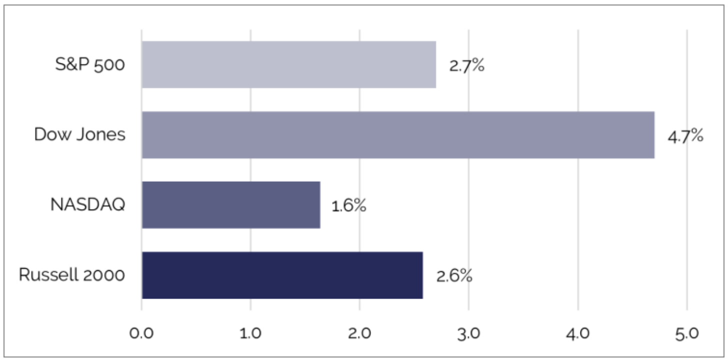
United Kingdom



In the UK the FTSE 100 index gained by 6.1% in the month to 8674, helped by the stronger US$; the FTSE 250 index of mid-sized companies was up by 1.6% and the FTSE SmallCap index by just 0.1%, while the FTSE AIM All-Share index was 0.2% lower.

The total return for the FTSE All-Share index including income was 5.5% in the period.

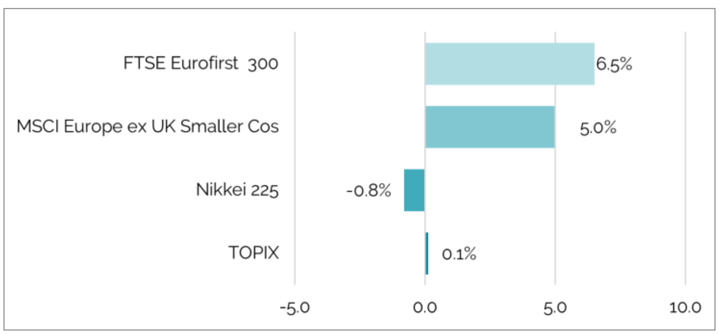
United States



In the US the S&P 500 index was up by 2.7% in the month, the Dow Jones Industrials index by 4.7% and the technology-oriented NASDAQ index a more modest 1.6%.

The Russell 2000 index of smaller companies was 2.6% higher.

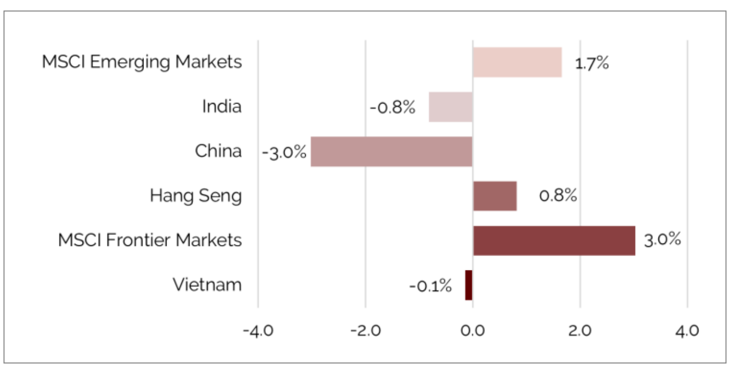
Europe & Japan



In Europe the FTSE Eurofirst 300 index was higher by 6.5% over the month, when the French and German markets were even stronger than those in Italy and Spain; the MSCI Europe ex UK Smaller Companies Index rose by 5%.

In Japan the Nikkei 225 index was down by 0.8% while the TOPIX index managed a small gain of 0.1%.

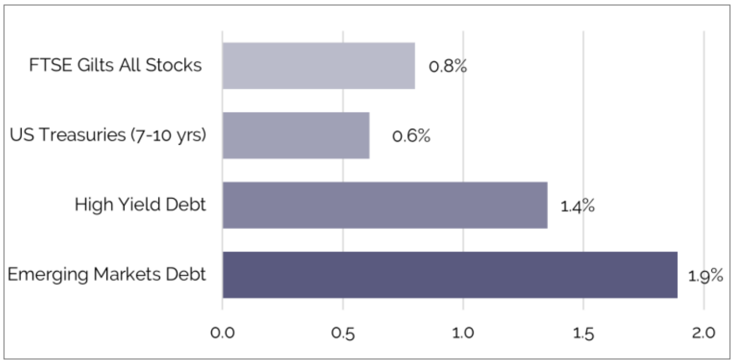
Emerging Market



The MSCI Emerging Markets index in US$ rose by 1.7% in the month, helped by a rise of 4.9% in the Korean market and a similar gain in Brazil. The Indian market was off by 0.8% and the Shanghai index by 3%, although the Hang Seng index in Hong Kong was up by 0.8%.

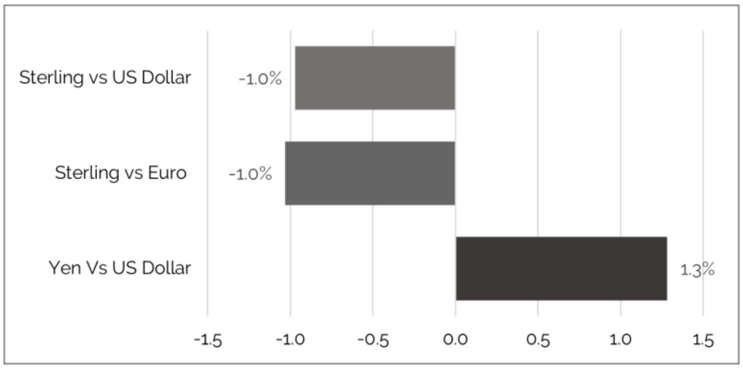
The MSCI Frontier Markets index was 3% higher although the Vietnamese market was down by 0.1%.

Bond markets



In bond markets the UK 10-year gilt yield was modestly lower at 4.54% from 4.57%, as was the US ten-year yield, and the total return for the FTSE Gilts All Stocks index in the month was 0.8%. In Germany the 10-year bund yield moved from 2.37% to 2.46%. There were positive returns in the major bond markets, with the best coming from emerging market debt.

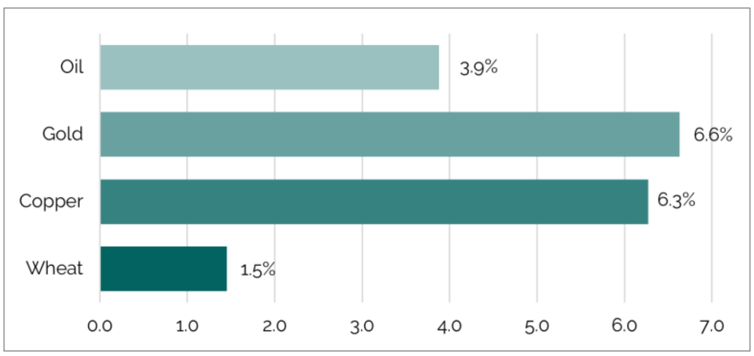
Currencies



Sterling was down by 1% against the US$ to close the month at a rate of $1.24:£, while against the euro Sterling was also off by 1% in the month to end at a rate of €1.20:£.

The Japanese yen rose by 1.3% against the US$.

Commodities



The price of Brent crude oil was 3.9% higher over the month to a level of $77 per barrel. The gold price reached new highs and rose by 6.6% to end the period at $2798 per troy ounce.

The prices of major metals were all higher in the month, with the bellwether copper up by 6.3%, while the main agricultural commodities were mostly higher, with wheat up by 1.5% and coffee up another 18.2%.

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