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INVESTMENT SERVICES

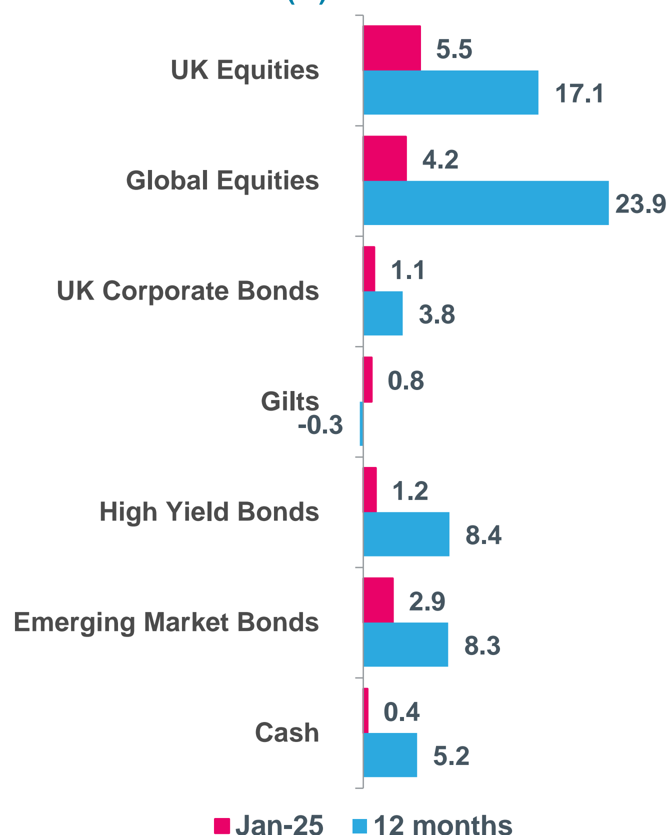
Hymans Robertson Investment Services (HRIS)

Market digest

January 2025

Monthly highlights

- A development in Chinese Artificial Intelligence (“AI”) models, as well as uncertainty of President Trump’s policies, led to a volatile but ultimately positive month for asset class returns.
- Equities led asset performance, driven by European and UK markets.
- On page 3 of this document, we provide market commentary to cover the 12 months to 31 December 2024.



Source: Morningstar. Figures to 31 January 2025. 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.
- It was an eventful start to the year. A powerful new AI model from a Chinese firm called DeepSeek was apparently built at far lower cost than US models, leading investors to reassess their AI holdings.
- Trump’s inauguration focused investors’ minds once again on the impact of his policies, especially tariffs.
- Despite the volatile nature of the month, equities had a strong start to the year. European equities were the standout performer with over 8% return as there were early signs of an economic recovery. A weaker pound also helped deliver strong performance for UK equities (as overseas earnings are now worth more in sterling terms).
- Bond markets started the month with a sharp increase in yields (bond prices fall as yields increase) as Trump’s policies are expected to add to US inflation. However, better than expected inflation data from the US and UK, and a “risk-off” response following the AI selloff, led to a rapid reversal with bond prices ending the month higher.
- 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

- President Trump fired the starting pistol on what could be a protracted trade war.
- Chinese firm DeepSeek is thought to have built an AI model of similar quality to the best US models and apparently at a fraction of the cost.

President Trump's tariff game has led to increased uncertainty and volatility

During the first weekend of February, President Trump announced that he was going ahead with tariffs on China, Canada and Mexico. The breadth and speed of the implementation took investors by surprise, as many expected the tariffs to be a negotiating tactic and for them to be more targeted toward certain industries. That assumption may still prove to be correct. After a bit of a stock market wobble on the Monday morning, Trump announced that the tariffs on Mexico and Canada would be postponed for a month after calls with their leaders – the China tariffs went ahead, however, markets partially recovered on news of the reprieve.

The episode was a bit of a wake-up call for investors, who may have thought that Trump was unequivocally good for markets. Trump's last-minute reversal seemed to confirm that tariffs are more of a political game than an economic one, which makes it more challenging for investors to read. For what it's worth, the UK may be one of the countries to face less direct impact. Firstly, the US has a trade surplus with the UK and so seems to be in Trump's good books. Additionally, only 15% of British exports make their way to the US, so if tariffs were to be enacted the overall impact would be small, albeit their impact may be more acute on certain industries like whisky.

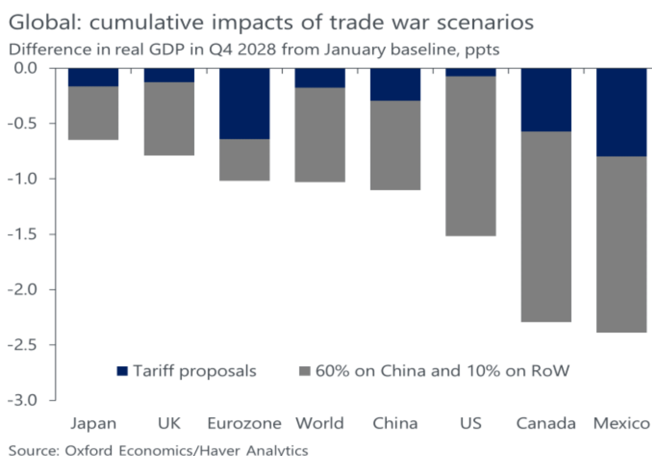
DeepSeek may change the economics of the AI industry

The realisation of the power, and the purported low build cost, of an Artificial Intelligence (AI) model from Chinese firm DeepSeek was also one of the key market events over January. AI has been one of the major investing themes of the last couple of years as large US tech firms, such as chipmaker Nvidia, have generated strong performance. The DeepSeek model threw into question the US' dominance and the assumption that billions of dollars of capital are needed to build the most sophisticated models. The market impact was quite narrow however, in that most stocks unrelated to AI were minimally impacted. Nvidia was the most affected major stock, falling 10% over the month. Still, it remains up 95% over the last year.

What this incident highlights, is how susceptible this area of the market is to corrections and volatility. It was also a useful reminder that the market-cap global equity index, where stock weights are determined by company size, is highly concentrated. As a result, performance of the market-cap index, and investments that purely track this index, are largely driven by a small number of stocks. To manage this concentration risk within our portfolios, we take a broader approach to regional allocation (i.e. not just follow the market cap index) and a more diversified stock exposure (i.e. utilise a range of managers and approaches).

Chart of the month

Forecast impact of trade war on various countries



This chart shows a forecast for the impact of tariffs on economic growth under two different scenarios – the current tariffs announced by President Trump, and another more extreme example.

Canada, Mexico and the Eurozone will be the most affected under the current proposal with GDP being between 0.5-1% lower by 2028 compared to a baseline.

Under the current proposal, and even a more extreme scenario, the UK will be one of the least impacted. Most of this is second order impacts like the effect of lower global growth.

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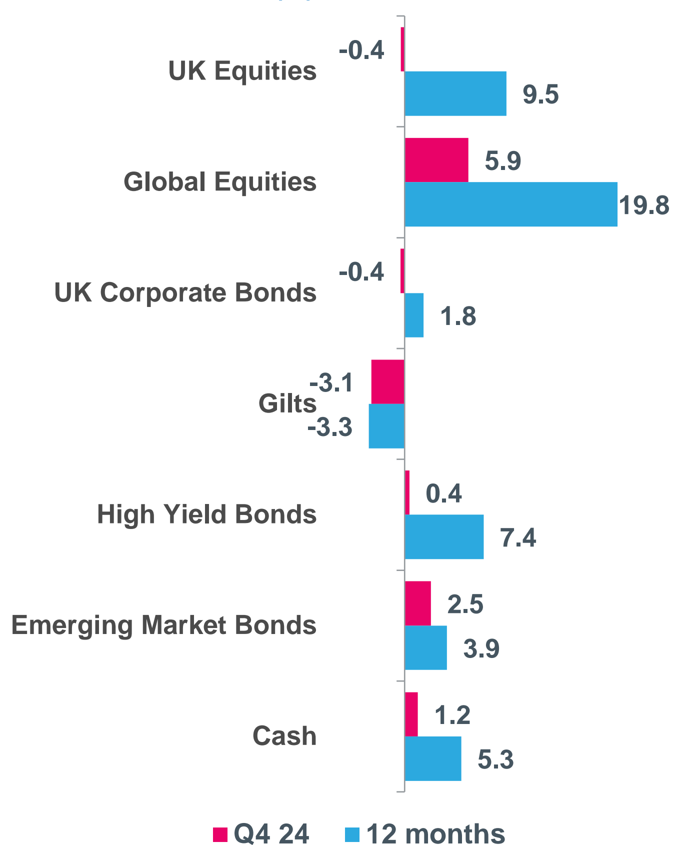
Annual market summary: covering the 12 months to 31 December 2024

The key question for investors going into 2024 was how fast central banks would start to reduce interest rates. Of equal importance was 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.



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.

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.

Risk warning

The value of your investments and the income from them may go down as well as up and neither is guaranteed. Investors could get back less than they invested. Past performance is not a reliable indicator of future results. Changes in exchange rates may have an adverse effect on the value of an investment. Changes in interest rates may also impact the value of fixed income investments. The value of your investment may be impacted if the issuers of underlying fixed income holdings default, or market perceptions of their credit risk change. There are additional risks associated with investments in emerging or developing markets. The information in this document does not constitute advice, nor a recommendation, and investment decisions should not be made on the basis of it. The material provided should not be released or otherwise disclosed to any third party without prior consent from HRIS.