JANUARY 2025

Market Outlook 2025:

NAVIGATING Shifting Landscapes

CIO Foreword

Years on, if anyone were to look back, 2024 would end up as an unremarkable year for many investors. Why? 2024 was unremarkable compared to how financial history remembers the likes of the 2000s housing boom, the roaring 90s, or 80s Reaganomics. It was also unremarkable in how certain high level market relationships played out: Stocks went up, stocks went up more than bonds, and US stocks went up more than international stocks.

Beneath the surface, things were far from straightforward. One's investment experience and outcome would have varied enormously depending on a few investment decisions such as Equity vs Bonds, Large vs Small-cap , US vs Rest of World, Value vs Growth. An investor in any of these camps would do well over time, but 2024 was a case where if one was not in US growth stocks, investing almost anywhere else was a drag.

One reason cited for this is the ongoing advancement in technology. One could be forgiven for saying "this time is different". How does one then invest in this "different" world? Amid all these changes, there are certain universal truths: that there are timeless human behaviour patterns that influence world events and markets. Such as the tendency to overestimate the impact of short term effects, and underestimate long term ones. So long as humans are part of the equation, no amount of AI will change this timeless human behaviour. To paraphrase the famous line from Mark Twain, "History never repeats itself. Man always does." What can one do then? By keeping up with the advancements yet also understanding what never changes.

Alvin Goh

Chief Investment Officer

THINK DIFFERENTLY

TO GET DIFFERENTIATED RESULTS

Market Outlook 2025: Navigating Shifting Landscapes

Executive Summary

2024 turned out to be a strong year for risk assets, with the S&P 500 once again leading the way. Robust returns were driven by resilient US economic growth, solid corporate earnings, and the continued dominance of the "Magnificent 7" stocks. Precious metals also had a stellar year, with gold delivering its best annual performance since 2010, supported by geopolitical concerns and central bank easing.

While US equities saw strong gains, other major markets delivered mixed results. Europe faced headwinds from high energy costs and weak exports, while Asia experienced a volatile year marked by the unpredictability of China equities. Despite a late-year rally spurred by stronger policy measures, China's lingering economic challenges remain a concern.

As we step into 2025, market sentiment is cautiously optimistic. Equities are positioned to benefit from a resilient US economy, with potential pro-growth policies under Trump's second term—such as tax cuts and deregulation—adding further tailwinds. As Trump's new term begins, we are watching closely for clarity on these policies and their potential impact. Overall, gains are expected to extend beyond the tech-driven leaders of 2024, as the AI narrative broadens into other sectors.

Opportunities also remain within fixed-income markets. For one, short-duration bonds continue to offer attractive yields that are less sensitive to volatile long-term rates. Such segments provide steady income, even as the outlook for additional Fed rate cuts may be less straightforward this year.

While the Fed's easing cycle has supported markets, the path forward will depend on evolving economic fundamentals. Persistent inflation, geopolitical tensions, and potential trade instability under Trump's administration are risks that could weigh on the outlook. Investors will need to remain agile to navigate these uncertainties effectively.

Reflecting on 2024, many forecasts had underestimated the strength of equity performance. As we look to 2025, current projections are more optimistic, but history reminds us that reality often diverges from expectations. As always, rather than relying solely on predictions, we focus on the fundamental drivers of markets—earnings growth, valuations, and economic trends—to guide our decisions.

Here's to a prosperous 2025 filled with health, wealth, and success in achieving financial goals! 🎉

MARKET REVIEW

We wish our readers a happy and healthy new year! To kick off our first commentary of the year, we review the key market developments of 2024 and share our outlook for the coming year.

2024 was another impressive year for risk assets though the anticipated Santa rally did not materialize.

S&P 500 suffered its steepest decline (>3%) from Christmas to the end of the year since 1952, as investors reduced their expectations for the pace of Fed rate cuts following a hawkish December policy meeting. Most of the decline happened over the last three trading sessions of the year when liquidity was thin. While US equities retraced since the December FOMC meeting, other "Trump trades" such as the long (stronger) US dollar maintained their strong momentum through the holiday period.

Despite the December pullback, 2024 was a strong year for markets. Precious metals and equities were the top-performing global assets, while other commodities lagged due to weak demand in China. 'Safe' government bonds disappointed with low to negative returns for the year driven by higher yields (recall the negative relationship between higher yields and lower bond prices).

The ongoing strength of the US economy contributed to the S&P 500's outsized 25% gain, in large part due to strong returns from the 'Magnificent 7' stocks which rose 67%. Meanwhile, a late surge in Chinese equities, along with robust performances from India and Taiwan, led to Emerging Market equities delivering high single-digit returns.

Amid central bank rate cuts and ongoing geopolitical concerns, precious metals had a strong year. Gold, in particular, saw its best annual return since 2010, rising by 27%.

2024 Performance	
Equities - S&P 500	25.0%
Equities - Magnificent 7	67.3%
Equities - Emerging Markets	8.0%
Precious Metals - Gold	27.2%
Bonds - Investment Grade (unhedged)	-1.7%
Bonds - Global High Yield	7.7%

Source: Bloomberg, FAM

US exceptionalism to continue in 2024?

The US not only avoided a recession in 2024 but also outshone other major regions in terms of economic growth and stock market performance.

In contrast, Europe faced economic challenges, particularly in the manufacturing sector, due to high energy costs and weak export demand, compounded by political turmoil in France and Germany. Consequently, European equities underperformed global equities in the past year.

In Asia, China's economic activity remained weak, but improved policy measures in September led to a late-year rally in Chinese equities. Lastly, Japan saw continued optimism over a weak yen and a steady economy supporting the Japanese equity market. While we have been concerned about the potential of a yen reversal hurting equities (a stronger yen tends to be harmful for the country's exporters), we are increasingly on the lookout for buying opportunities to take advantage of continued corporate reforms in Japan.

Fed easing cycle…

The underperformance of government bonds was a major surprise for many - the majority of advisors surveyed a year back were expecting bond yield to fall in 2024 (i.e. higher bond prices). With falling inflation and anticipated Fed rate cuts, 2024 was projected to be a highly favourable year for long-duration bonds.

…at risk of a pause?

The long-anticipated Fed easing finally started in September 2024, with the Fed's initial outsized 0.5% cut fueled by weaker-than-expected Non-Farm Payroll data released in early August. However, this has proven to be just a blip with the US remaining resilient through the rest of the year. Furthermore, the breach of the 'Sahm Rule' (the infamous recession indicator) in August was seen to be driven more by stronger labour supply due to the high rate of immigration as opposed to mass layoffs happening. In short, both labour market and economic growth remained resilient in the US. This increases the risk of a Fed pause materially over the next few months.

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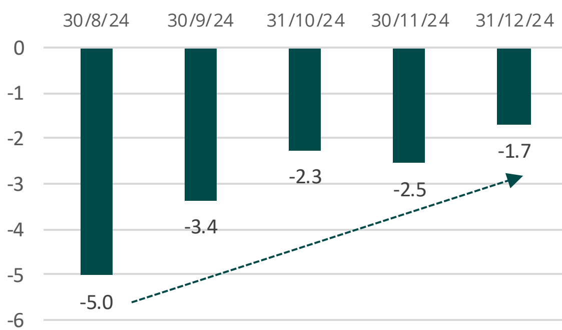
MARKET REVIEW

Consequently, the stronger-than-anticipated US economy hindered government bond returns as expectations for future Fed rate cuts were scaled back meaningfully. The number of rate cuts expected has come off from 5 in August to ~1.7 by the end of December 2024. We are on high alert for any further indications of a pause in the rate-cut cycle going forward, especially with Fed chair Jerome Powell signaling that they will take a more cautious approach when considering further interest rate cuts.

Number of rate cuts expected in 2025



Source: Bloomberg, FAM.

Longer-term bond yields actually rose following the Fed's initial rate cuts in September (this is what happens when expectations meet reality). Notably, the 10-year Treasury yield rose for the 4th consecutive year, a phenomenon not seen since the 1980s. Besides government bonds, this also had implications on longer-duration investment-grade credits which also lagged due to rising bond yields – so much for higher credit ratings!

Meanwhile, the lower-rated global high-yield bonds returned 7.7% thanks to attractive all-in yields and tighter spreads.

Looking ahead into 2025

Equities: There is a good chance that global equities will continue to do well. The current positive economic backdrop, with the AI-narrative expanding beyond mega-cap tech is overall supportive for risk-assets. In the US, potential tax cuts and de-regulation could also boost corporate earnings, justifying elevated valuations (for now) and allowing for further gains here.

Bonds: On the other hand, we continue to see limited upside to longer-dated bonds with lower relative yields and volatile interest rate path (though they would do quite well if we see a recession; a lower probability event for now). Within fixed income, we continue to like shorter-duration bonds that are still offering attractive yields to income investors.

Within our flexible multi-asset strategy, we like holding gold as a diversifier to hedge against inflation and geopolitical risks into 2025.

In the near term, the path of least resistance is for markets to be rangebound up till Trump's inauguration on January 20th. More clarity on US policy is required to navigate through Trump's second term, to determine if the same drivers of performance will remain in play.

Risk assets outperformed as economic growth surprised on the upside and central banks began to cut rates

US Exceptionalism

Gold shines bright

Central banks cut rates

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NEW YEAR, NEW TARGETS

This is the time for many to set and embark on new targets for the year. Gyms are likely to be unusually crowded these next few days as many are motivated to get a head start on their fitness goals for the year. Likewise, this is also the time for Wall Street strategists to come out with their market forecasts for 2025. While it may be interesting to compare these targets relative to your own expectations, investors should remember that such forecasts are far from the crystal balls that many think them to be.

As mentioned earlier, 2024 was a particularly good year for the S&P 500. Let's see how actual returns compared to what forecasters were expecting at the start of the year:

	Forecast	
Median	2.2%	
75th Percentile (Bullish)	6.9%	*e.g. Goldman Sachs*
25th Percentile (Bearish)	-2.6%	*e.g. Wells Fargo*

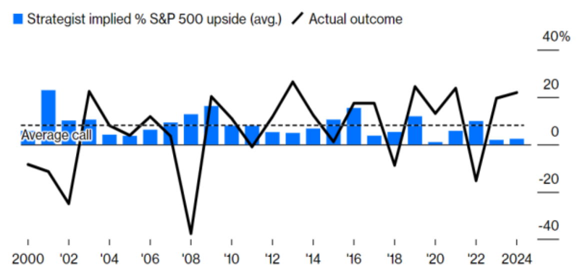
It turns out that forecasters did not predict much upside in 2024; with the median forecast a mere 2.2% (even less than cash returns!). In contrast, the S&P 500 eventually ended the year with a 25% return. The bearish forecasts were predicated on fears of a weakening consumer and deteriorating economic environment which did not pan out in the end.

What are forecasters expecting for 2025? It turns out that they have gotten more bullish after the good performance in the past year: the median forecast for 2025 is now 12%:

	Forecast	
Median	12.2%	
75th Percentile (Bullish)	13.9%	*e.g. HSBC*
25th Percentile (Bearish)	10.5%	*e.g. Goldman Sachs*

Source: Bloomberg

How much should we pay attention to these forecasts? Historically, these targets (below in **blue**) have tended to be quite different from actual outcomes (**black** line); reminding us that is difficult for anyone to consistently predict short-term market performance. Actually, it is much easier to predict long-term market performance; but we'll leave that discussion for another day.



Source: Bloomberg

That said, all of these forecasts are not for nought. Long-time readers would know that we preach 'looking under the hood' of any investment before investing. The same can be applied here – underpinning these forecasts are valuable insights into the fundamental drivers of market performance. We prefer to follow these market drivers closely rather than relying on forecasts to invest:

2024: Initial bearish forecasts ended up being too bearish as inflation continued to cool, the Fed cutting interest rates, and the economy ultimately avoiding a recession. This was a challenging environment, but one that flexible and nimble investors could take advantage of. Likewise, we took a defensive posture prior to the August 2024 sell-off as economic data moderated, and added back into US equities as Trump's win increased the odds of stronger economic and corporate earnings growth in the US.

2025: This year looks to be one of cautious optimism. Market valuations remain stretched after the gains in 2024, but they may remain so until we see clearer signs of recession (still not the base case). Meanwhile, lower interest rates and pro-growth policies support the broadening of gains beyond the narrow group of tech stocks that has been driving returns over the past year – in all supportive for markets, but we pay close attention to the risk of another trade war that cast a shadow over the more optimistic base case.

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SHIFTING GEARS ON INCOME

Income markets were underwhelming
In 2024, the common strategies for income investors did not fare well relative to even money market funds (cash). A generic 30/70 (equity/fixed income) strategy returned 4.3% while the popular Investment Grade (IG) market returned 3.4% before fees. The return for investment grade is not a surprise; yields at the start of 2024 were 3.5%, so an IG investor should not have expected more. It was with this in mind that we positioned outside of these popular markets at the start of the year…

*Segment & performance	2024
Typical income strategy 30/70	4.3%
Popular Investment Grade market	3.4%
Money Market Fund	5.2%
Developed Market High Yield	8.2%
Asian High Yield	15.1%

Our income strategies outperformed
… which resulted in a relatively good year for FAM's income strategies. Whether it was in traditional or alternative markets, our income funds closed the year at almost 10%. Outperformance in traditional markets came from our exposures to high-yield markets, specifically in Emerging Markets and Asia.

AHY provided income and capital gains
Was it a surprise that Asian High Yield (AHY) returned 15%? Depends on whom you ask: Anyone who was surprised was probably pessimistic after extrapolating the lacklustre single-digit performance in 2023. For us, it was less of a surprise as AHY yields started 2024 at 12.5%. Not only did AHY investors get the yield, but they also got some capital gains. It was akin to picking up dollars in an uncrowded open field.

Income: US exceptionalism was the exception to the rule
2024 was notable for US exceptionalism: Large-cap US stocks were one of the year's biggest stories. But this was not true for income investors: European and Emerging market credits outperformed the US.

Why did US credit underperform?
A host of factors cited include weaker credit fundamentals and renewed concerns about financing wall amid a higher funding cost environment. Perhaps the answer is simpler: The strong gains in 2023 for US credits attracted new investors, pretty much the opposite of picking up dollars in an uncrowded field.

This is an appropriate juncture to remind ourselves of how the timeless human response can be at odds with what one should do logically to achieve their investment goals. It's not just because investors are figuring out how to position for 2025, but also because the risk-reward in credit markets has shifted.

	Human response	Logical response
Price goes up	"It must be good, let's add"	Reduce exposure to sell at higher prices
Price goes down	"Something must be wrong, let's cut"	Add exposure to buy at lower prices

Some may be keen to add to AHY on the back of strong performance; after all an investment that outperformed must be good.

Not outstaying welcome: Shifting gears
In the current environment, we're more inclined to start taking money off the table on Asian high yield, and broadly high yield. High-yield markets globally are yielding less than 8%. This means that while one can still get a higher return in high yield compared to cash, there is less potential for capital gains while being exposed to more volatility.

Unlike the period of close to zero interest rates in the prior regime, it is not as crucial today to overstretch for high yield to get income. Having benefitted from high-yield markets, we are gradually shifting our fixed-income positions up in quality without giving up too much yield. We believe that 2025 will be another good year for income investors, but it requires a more delicate balance between earning income and mitigating volatility.

*Source: Bloomberg. 30/70: Bloomberg Global 30:70 Index, Investment grade: Bloomberg Global Aggregate Index, Money market fund: Vanguard Federal Money Market Fund, Developed market high yield: ICE BofA US High Yield Index, Asian high yield: Bloomberg Asia USD High Yield Bond Index

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HOW ARE WE POSITIONED?

Equity (Green) **Bonds (Blue)**

Key Themes	Allocation
US Exceptionalism + Growth Broadening Economic resilience in the US (vs rest of world) supports the continuation of 'US exceptionalism' at least in the near-term. President Trump's second term also comes with the prospect of tax cuts and de-regulation which would support risk-assets – we await more policy clarity as Trump takes office. There is also a case for returns broadening out beyond the narrow group of tech-related stocks - globally and also within the US -, supported by steadier economic growth going forward.	**US equities** **Global equities** (e.g. Europe, Japan)
Diversification Into Emerging Opportunities Financial markets operate in cycles. The end of the easy money era means looking beyond popular markets that did well during the previous broad-based growth to find tomorrow's winners. Focus on high-growth markets driven by their own distinctive economic trajectories and coupled with attractive valuations.	**Emerging Market equities** (e.g. China, India, Vietnam)
Shifting Gears On Income Having benefitted from the strong performance of high-yield bonds, we are gradually transitioning to higher quality fixed income positions while maintaining attractive yields. Investors can still achieve solid income in today's environment but requires a more careful balance between generating returns and managing volatility.	**Developed-Market Credit** **Asian High-Yield Credit** **Emerging Market Credit**

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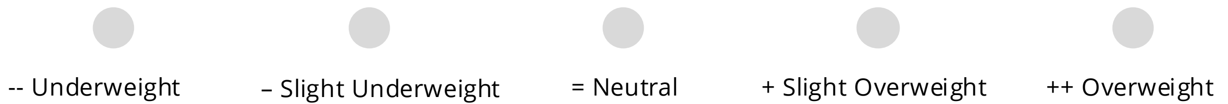
ASSET ALLOCATION STRATEGY



-- Underweight – Slight Underweight = Neutral + Slight Overweight ++ Overweight

Equity: Regions

United States

Economic resilience coupled with the prospects of favourable policy i.e. tax cuts supports the continuation of good performance in the US. Maintaining an overall higher quality positioning as valuations remain stretched.

Europe

Europe's pro-cyclical industrial base to benefit from steadier economic growth so long as severe recession is not on the cards.

Japan

Current lower exposure reflects concerns of potential yen reversal hurting equities. That said, we are on the lookout for attractive entry points to take advantage of continued corporate reforms in Japan.

Asia Pacific ex Japan

More pro-active stimulus measures embarked by the Chinese government provides better tailwinds for Asia equities. Currently participating in Asia and China via broader exposure to Emerging Markets.

Emerging Markets

Maintain preference for high-growth markets at attractive valuations i.e. China and Vietnam.

Fixed Income

Global

Focus on government bonds' flight to quality characteristic to buffer portfolio volatility during periods of stress.

Investment Grade Corporate

Maintain a diversified exposure and taking advantage of mispricing opportunities in developed-market investment grade bonds.

US High Yield

Maintaining minimal exposure due to as IG bonds offer relatively better risk-reward to obtain income while mitigating default risk.

Asia

While Asia credit continues to offer attractive all-in-yields and supportive fundamentals, we maintain a neutral allocation after realizing strong income and capital appreciation.

Emerging Markets Debt

Hard currency bias to focus on return from credit while limiting exposure to emerging market currencies. Short-duration bonds to mitigate volatility from more uncertain interest rate path.

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MARKET INDEX RETURNS

Equity Regional	MTD	YTD	10Y	20Y
Global	-2.34	18.03	9.81	8.24
United States	-2.39	25.00	13.09	10.35
Europe	-2.50	2.54	5.89	5.88
Japan	-0.99	7.92	6.58	4.47
Asia Pacific ex Japan	-1.15	10.15	4.66	6.75
Emerging Markets	-0.12	7.97	4.02	6.35

Equity Markets	MTD	YTD	10Y	20Y
Australia	-8.15	1.99	6.95	8.21
Brazil	-6.46	-29.55	0.30	3.45
China “A”	-0.14	15.03	1.67	9.91
China “H”	5.12	32.13	-1.32	5.60
Hong Kong	3.45	23.58	1.91	5.32
India	-3.26	6.55	9.07	10.88
Indonesia	-2.29	-3.66	3.03	10.03
Korea	-7.42	-19.93	1.18	5.02
Malaysia	2.50	20.66	0.39	5.98
Singapore	-0.76	19.17	5.00	7.44
Taiwan	2.72	22.80	13.12	10.63
Thailand	-1.58	2.24	2.06	8.25
Vietnam	0.94	8.82	9.26	8.79

Equity Sectors	MTD	YTD	10Y	20Y
Gold	-8.58	10.64	7.69	2.71
Energy	-9.47	5.72	4.86	7.18
Technology	0.74	33.10	20.22	13.84
Healthcare	-6.05	1.61	7.87	8.98
Financials	-5.46	30.50	11.38	5.59

Fixed Income	MTD	YTD	10Y	20Y
Global Aggregate	-2.15	-1.69	0.15	1.86
Global Aggregate (H)	-0.77	3.40	2.01	3.34
High Yield	-0.49	7.65	4.70	6.23
Asia	-1.16	3.68	2.88	3.18
Emerging Markets	-1.19	6.58	3.20	5.49

Note: (H) Currency Hedged

Currencies	MTD	YTD	10Y	20Y
SGD/USD	-1.93	-3.33	-0.30	0.89
EUR/USD	-2.11	-6.21	-1.54	-1.34
JPY/USD	-4.73	-10.28	-2.69	-2.11

Commodities	MTD	YTD	10Y	20Y
Gold	-0.71	27.22	8.28	9.36
Oil	5.47	0.10	3.02	2.54

*As of 31 Dec 2024. Source: Bloomberg. **Total return in USD**.*
10 and 20 year returns are annualized.

"In investing, what is comfortable is rarely profitable."

Rob Arnott

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