Canaccord Genuity Wealth Management

MPS investment update

January 2025 (written 7 January 2025)

Portfolio asset allocation

	Risk profile 3	Risk profile 4	Risk profile 5	Risk profile 6	Risk profile 7
Debt and fixed interest	**58.47**	**46.07**	**31.39**	**16.60**	**0.00**
Emerging Markets	3.02	2.99	2.02	0.00	0.00
International	10.97	11.89	8.83	4.36	0.00
Government	21.20	12.94	8.12	3.81	0.00
Corporate	23.28	18.25	12.42	8.43	0.00
Equities	**20.60**	**40.75**	**60.70**	**80.68**	**97.74**
Emerging Markets	1.00	1.97	1.95	2.64	2.87
Far East	1.02	2.02	2.21	3.86	4.80
Japan	1.05	1.12	1.96	2.55	3.09
North America	3.35	7.97	11.61	16.79	20.79
Thematic	2.11	3.97	6.73	8.11	8.51
United Kingdom	6.37	12.31	18.99	25.38	31.12
International	5.70	11.37	17.24	21.34	26.56
Alternative investments	**14.91**	**10.15**	**5.01**	**0.00**	**0.00**
UCITS funds	12.89	8.17	2.95	0.00	0.00
Commodities	2.01	1.98	2.06	0.00	0.00
Cash	**6.03**	**3.03**	**2.90**	**2.72**	**2.26**

Data as at 31 December 2024

Core inputs to our asset allocation framework

The economy

There are still no obvious signs of a global recession in 2025, though the economy is mixed. It sounds repetitive, but the US remains 'exceptional' with strong rates of growth, Europe is broadly stagnating and China has stabilised at a low growth rate. We should probably expect these trends to persist in the early part of 2025. What could shift this dynamic? A potential slowdown in US consumer activity, though that seems difficult to imagine currently, or a more progressive approach to stimulus in China, which could support a tentative recovery in global manufacturing. For now, we expect the 2024 status quo to continue but will be monitoring developments closely.

Inflation

Inflation continues to be less of a problem than it was in 2022 and 2023, though rates have stalled between 2.5% and 3.5%. We anticipate inflation rates will drift slightly lower in 2025, but returning to central bank targets of around 2% will be challenging. Our long-held view has been that a 2% inflation rate will be the minimum this decade, unlike the maximum it was in the last. Risks remain, particularly if the Trump administration's more extreme policy proposals are realised. As with economic growth, we will have to wait and see.

Interest rates

There's tempered expectations for interest rate cuts in the US and the UK, as economic activity in the US has been solid while inflation in the UK is persistent. Current pricing in futures markets (a marketplace for buying and selling contracts to trade assets at a future date and price) imply that we will see between two and three further rate cuts in the next 12 months, which does not seem wildly incorrect to us. In the US, many commentators believe that the Federal Reserve should now be 'on hold', as they await further evidence on economic activity and inflation, as well as government policies. We think this is appropriate over the next few months.

Corporate earnings

As the new year begins, so does another corporate reporting season, as companies reveal how they fared in the final quarter of 2024. Results are expected to be positive, with earnings and revenues growing and profit margins expected to widen. The same trends are expected in 2025. Economic growth, US government policies and falling interest rates should support earnings growth in 2025, though unmet expectations could weigh on overvalued US equities, where optimism and complacency runs high.

Valuation and positioning

This monthly commentary risks being repetitive, but here we go again. US equities remain historically overvalued but are supported by strong corporate performance and robust earnings growth. Still, it's worth questioning if the optimism has gone too far. In contrast, equity valuations in Europe, Asia, and the UK are either modest or outright cheap, leaving room for significant recovery if positive surprises arise. Bond market valuations appear fair given the outlook for growth, inflation, and interest rates. One concern is narrowing corporate credit spreads (the yield difference between corporate and government bonds of similar maturity), though this reflects corporate strength, positive earnings prospects, and high demand for fixed income investments.

Key subject of the month: 'Our key investment areas for 2025'

- We are moving from the predictable 'great moderation' of 2024 to an uncertain 'great unknown' in 2025
- 2024 was a good year for investors, with fixed interest, equities and alternatives posting positive returns
- The distress from the nadir of investment portfolios in late 2022 is fading from investors' memory, and the recovery from those lows has been robust
- Can this positive environment for investors continue in the year ahead?
- While the widespread cheap valuations seen after the summer 2022 market sell off are no longer prevalent, many attractive opportunities remain
- We are attracted to the shorter maturity end of government bond markets, as yields remain elevated; in the UK, there is still the opportunity for tax-efficient returns in bonds that are trading below par
- We are also optimistic about our ability to harvest good returns in areas of corporate and consumer credit
- Lower inflation, positive economic growth and lower interest rates should be a good backdrop for credit: specific areas like asset-backed securities and short-dated financials bonds could well be key drivers of outperformance again
- In equity markets - despite macroeconomic uncertainty - high quality, defensive companies are historically cheap: sectors like consumer staples and healthcare could prove excellent risk/adjusted opportunities
- The UK market is ignored by investors and there is a case to be made to embrace UK small and mid-cap-sized companies, which could prove a classic contrarian opportunity, just as everyone is giving up
- The US and Japanese equity markets offer many world-leading companies at sensible valuations and we expect these to be strong areas of corporate profits growth in the year ahead
- Our alternative allocations provided dependable and rewarding in 2024 and we expect them to contribute positively to portfolios in 2025's volatile environment
- As we have hopefully made clear, having any real degree of certainty over the macroeconomic outlook is hard - but the comforting range of attractive investment opportunities on offer creates as much certainty as possible.

Key asset allocation positioning

- We are still neutral in all asset classes at a 'headline level', reflecting our view that most asset classes are offering a fair balance between risk and reward
- This view has remained consistent over the past 15 months, and while we believe it remains appropriate for early 2025, we stay open-minded given the potential unpredictability of the year
- We persist with a moderate underweight stance towards the US, large cap tech and growth themes in equity markets, although we have moderated that underweight stance
- We still admire the value opportunities in regions like Asia, Europe, and the UK, although we do not have an extreme positional skew
- While our equity allocation is neutral, we believe that we are well placed for a potential economic slowdown, as we have increased focus on those companies that should have dependable business models and profit streams in a slower economic environment
- We remain underweight UK gilts and interest rate duration in fixed interest investments but have moderated our previous positioning and are expecting to increase interest rate sensitivity further
- Our consistent view over the past 15 months remains appropriate as we head into early 2025, though we stay open-minded given the potential unpredictability of the year ahead
- Alternatives can add value in volatile markets, as 'relative value' trades help, but we can now find better opportunities elsewhere in fixed interest and equity markets
- As stated repeatedly through the last few years, our key stance is to remain balanced, diversified and operating with a 'flexible mindset'.

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