Global Markets Overview

Asset Research Team

December 2024

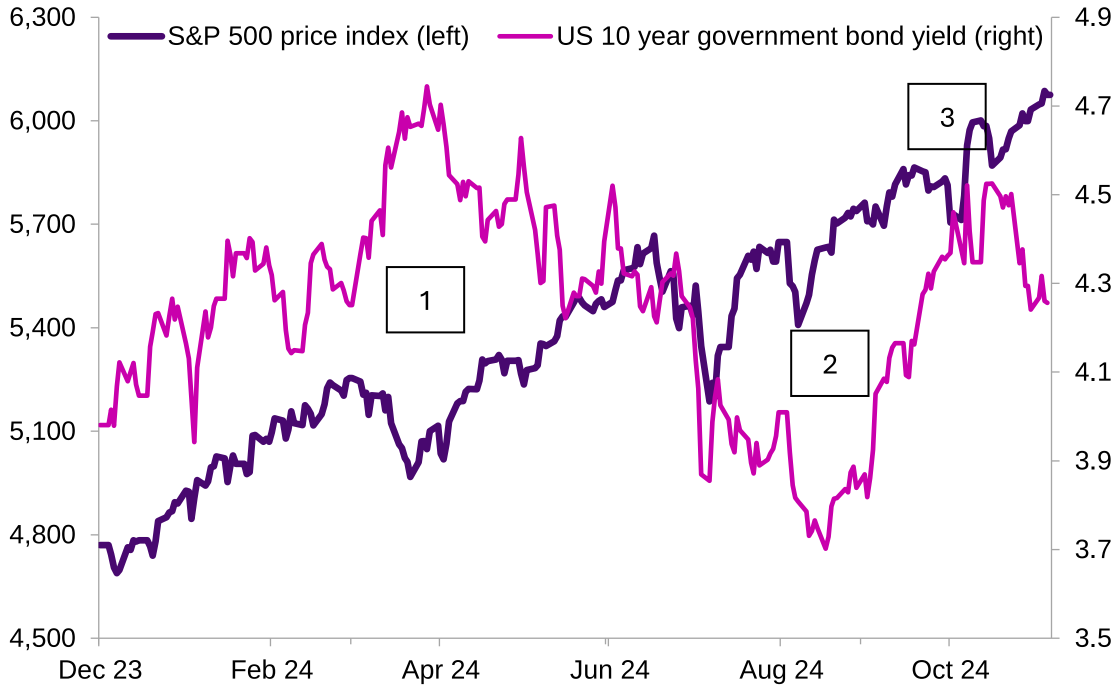
Chart of the month

As we approach the end of the year, it is useful to look back at the key macro and financial market developments over 2024. Our Chart of The Month looks at broad US equity performance over the year to date as well as the 10-year US government bond yield.

1. **In January to April 2024**, US GDP growth started picking up to high rates of growth, after having slowed for most of the second half of 2023, albeit from exceptionally high levels. At the same time, month-on-month US core personal consumption expenditures inflation also increased, having been low in November and December the previous year. US equities benefited from the increased confidence in the growth outlook, rising materially. However, the combination of reaccelerating and strong growth, and higher inflation and inflation concerns, pushed up US government bond yields to their year high.
2. **In May to October 2024**, the US inflationary picture flipped over, with month-on-month US inflation slowing. Investors became increasingly confident that the US labour market and wider economy was normalising and inflation falling towards the Federal Reserve target – a 'soft landing.' The Federal Reserve shifted to emphasising that it saw growth and inflation as slowing, and policy as restrictive, and would look to cut gradually. Bond yields fell and the first US interest rate cut of this economic cycle followed in September. At their lowest point in September, US bond yields were pricing in around 2% worth of interest rate cuts over the following year. As is often the case at policy inflection points, bond markets had got ahead of themselves, which led to an appropriate partial rise or normalisation of US bond yields in October/November. The U.S. equity market continued to surge on optimism surrounding artificial intelligence (A.I.) and the continued strength of US consumer spending.
3. **Leading up to November and after** the election of former President Trump was a key driver of markets, with investors weighing up possible outcomes in Trump's key policy areas: including tariffs on imports from Canada, Mexico, China, and Europe as well as corporate tax cuts for US companies. Over November, we saw European equity markets down slightly and US equities outperforming global equity markets, reflecting expectations that these policies, in aggregate, may benefit US listed companies more so than international counterparts. Overall, the S&P 500 has gained nearly 27% year-to-date, with US large-cap technology companies driving this growth.

The moves in US equities and US government bonds over 2024

S&P 500 price index and US 10-year Treasury yield



Sources: FactSet, WTW

Government bonds

At current yield levels we believe most bond markets are neutrally priced

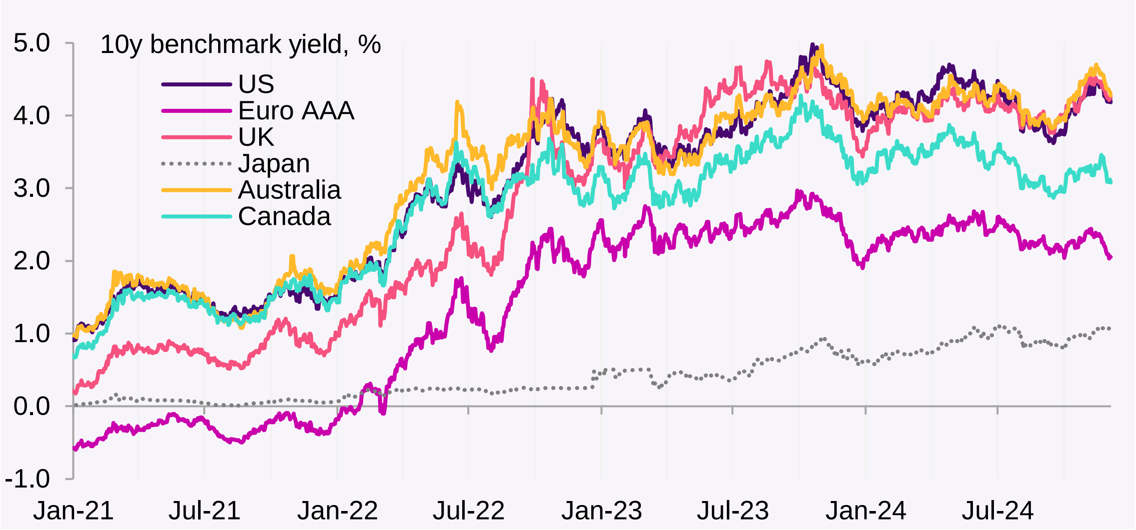
What happened over the past month:

Global bond yields (prices) have, generally, fallen (risen) over the past month, with some variation across markets. German 10y yields have fallen the most since the start of November (as of 4 Dec), declining 34bps, while Japanese equivalents rose 11bps. US 10y Treasury yields dropped roughly 10bps.

Factors influencing market trends

Bond markets remain highly sensitive to economic data and policy. After rising over the previous month, US yields stabilised and fell In November. In Europe, economic weakness, notably in Germany, drove yields lower. November's HCOB Manufacturing PMI figure – a survey of business spending intentions – for the Eurozone was suggestive of a worsening contraction, while the number for the services sector shifted from expansionary towards contractionary territory.

Global 10-year benchmark nominal bond yields



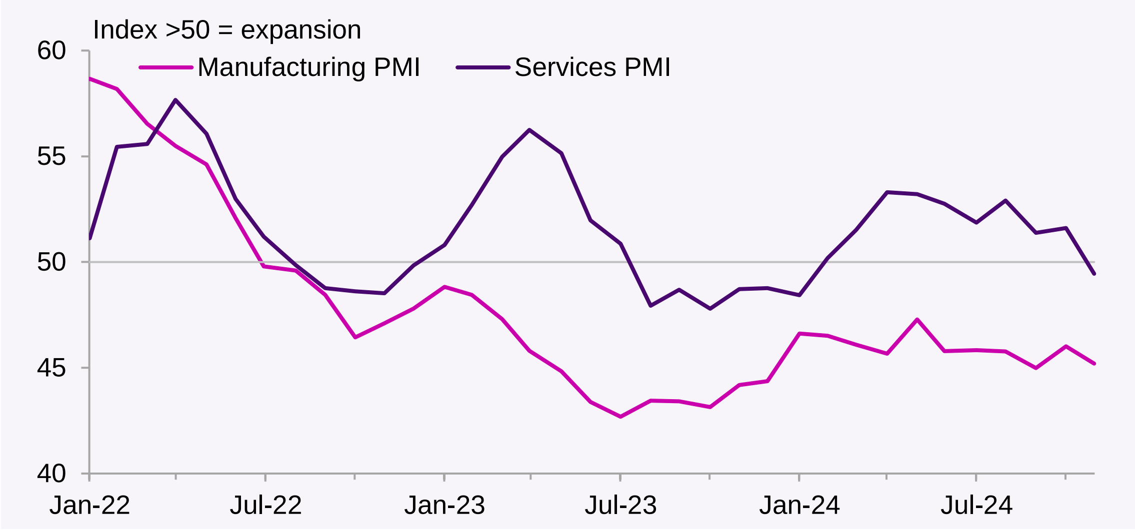
Sources: LSEG Datastream, WTW

Looking ahead:

We expect bond yields to remain volatile in the near term. US bond markets, which impact global bond markets, will remain focused on updated policy proposals from President-elect Trump. The impact on growth, inflation, and financial markets will, ultimately, be contingent on the actual policies that are implemented.

In 2025, we expect inflation and growth to moderate, allowing central banks to ease policy. However, the speed and depth of that easing cycle will vary by country. **We think that most bond markets are neutrally priced over a one to three-year horizon**. Although, they continue to have a valuable role in protecting return-seeking portfolios. **For under-hedged liability-driven-investment portfolios, current pricing remains reasonable to return towards target levels**.

Euro area PMI figures indicate economic weakness



Sources: FactSet, WTW

Credit

Over five years we expect investment grade credit to outperform government bonds moderately

What happened over the past month:

In a good month for corporate assets overall, November saw corporate credit spreads decline in almost all major markets. However, the current narrowness of spreads limited significant gains and the fall in spreads was less than October. Additionally, equities significantly outperformed credit, even after adjusting for their higher risk. Global investment grade credit spreads fell by 2 bps to 90bps. With spreads in the US, UK, Canada, and Australia all falling over the month. It was a mixed picture in global high yield markets, with spreads falling significantly in the US but rising in Europe – the same directional performance as equities.

What has influenced recent market dynamics?

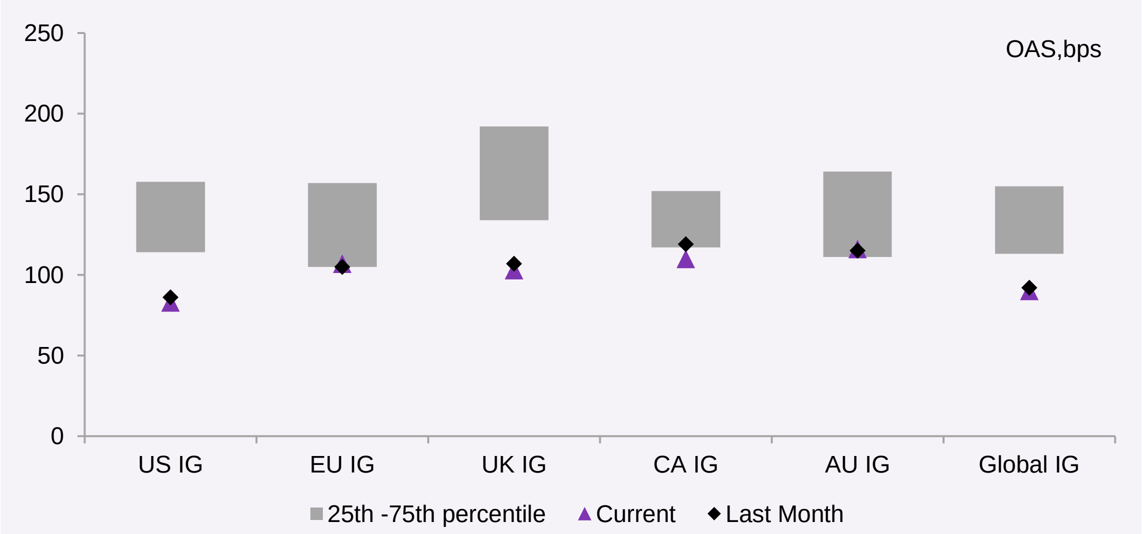
Relatively **healthy interest coverage ratios** and **a notable phase of corporate issuers terming out their debt maturities** prior to the recent rate hiking cycle has cushioned corporate credit markets from the slowdown in economic growth in some advanced economies (e.g., the Eurozone). The exceptional strength of the US economy has also been a notable support. Our outlook is for US growth to continue to provide support to credit markets throughout 2025, given the expansionary stance of new President-elect Trump's overall policy mix. As a result, the **non-financial corporate downgrade and default cycle has been relatively benign throughout 2024** and we expect this to continue through 2025.

Looking ahead:

Over a three-to-five year horizon, we expect global investment grade corporate credit to provide only moderate returns above government bonds. Similarly, we expect global high yield credit to only slightly outperform government bonds and investment grade credit over the medium-term.

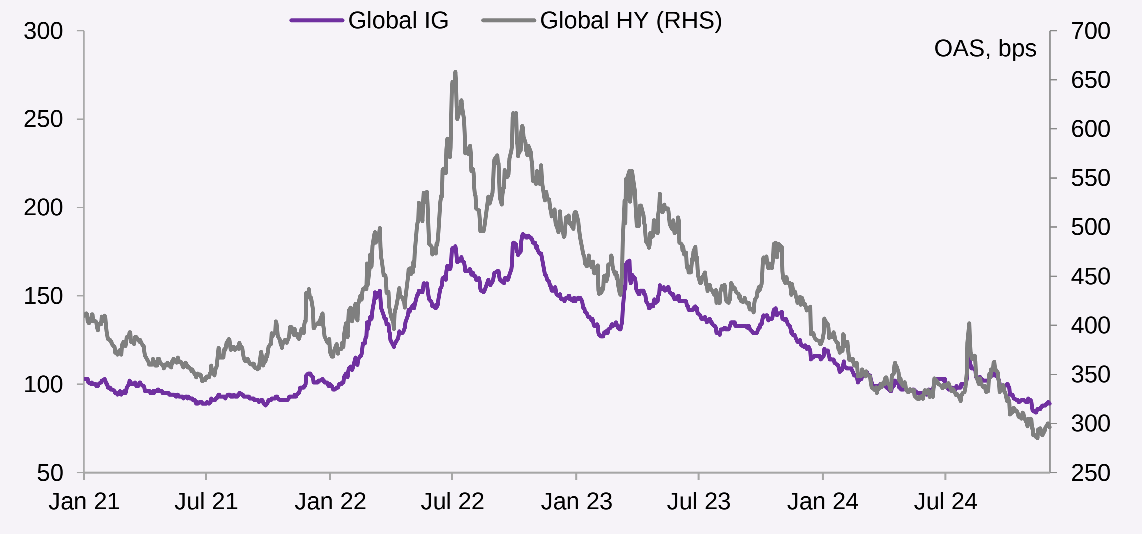
We are balanced over 2025, given good underlying macro and earnings conditions, in the US especially, which nets off against the narrowing of corporate credit spreads year-to-date and their low levels currently.

Investment grade spreads by country



Sources: FactSet, WTW

Both credit spreads and company debt measures show little sign of corporate stress



Sources: FactSet, WTW

Equities

Overall, we retain a neutral view on equities over a five-year horizon

What happened over the past month:

Global equity markets gained 2.6% in November in total return terms, driven by strong US equity performance. The strengthening US dollar, which reduces global returns in US dollars, was more than offset by investor optimism following a decisive US election outcome and expectations of corporate tax cuts and deregulation in the US. Euro area equities fell by 1.3% over the month, partly driven by investors weighing up potential tariff impacts. Emerging markets also underperformed over the month, pressured by trade policy uncertainty, US Dollar strength, and the potential impact of a less accommodative monetary environment. In Asia, markets fell amid US tariff threats and China's fading stimulus-driven optimism. Overall, developed markets outperformed emerging markets by 6.6% over the month.

Broad market trends:

Looking to forward earnings, analysts forecast earnings picking up significantly in 2025, particularly in the US. However, our outlook for inflation remaining close to central bank targets, good economic growth in the US, and a gradual easing of monetary policy in advanced economies, should support stock prices. We remain balanced in our outlook for equity returns over the remainder of 2024 and 2025.

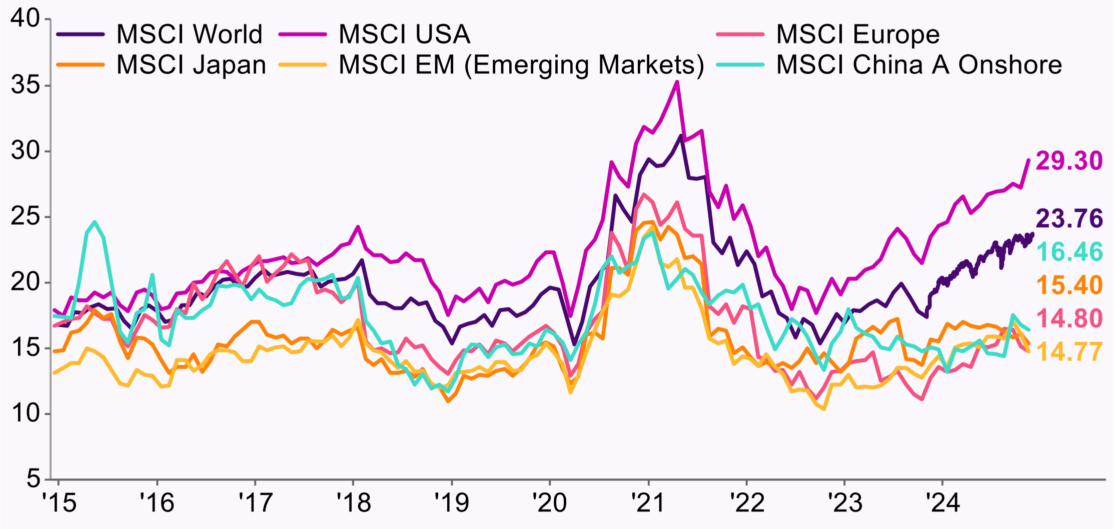
Over the last three months, the top performing sectors have been Consumer Discretionary (13.5%), Financials (10.8%) and Communication Services (9.7%).

Looking ahead:

Overall, we retain a neutral view on equities over a five-year horizon. In the shorter-term, we see value in Japanese equities and US small caps given the positive impact on fundamentals of stimulative monetary policy and good cyclical economic growth conditions.

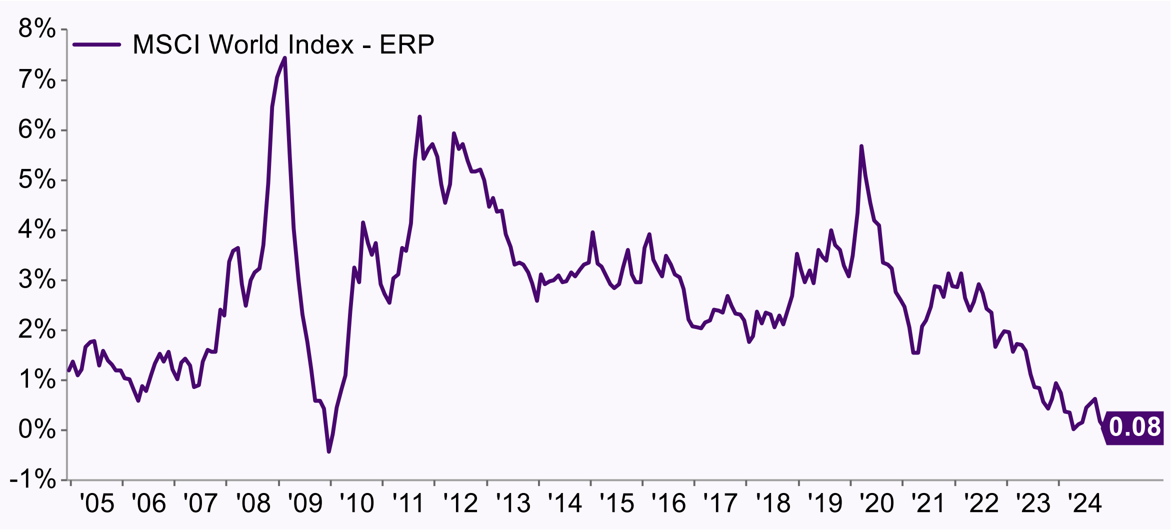
Global equity valuations

Trailing price to earnings ratio



Sources: FactSet, WTW

A measure of the Equity Risk Premium remains low



Sources: FactSet, WTW

FX

We hold a positive view on most developed currencies relative to the US dollar over the long term

What happened over the past month:

The US dollar has continued to strengthen against the major currencies. Since the beginning of November, the dollar has appreciated c. 3% against the euro, and 1% to 2% against the Australian dollar and British pound (as of 4 Dec). Bucking this trend was the yen, which rose against the US dollar slightly.

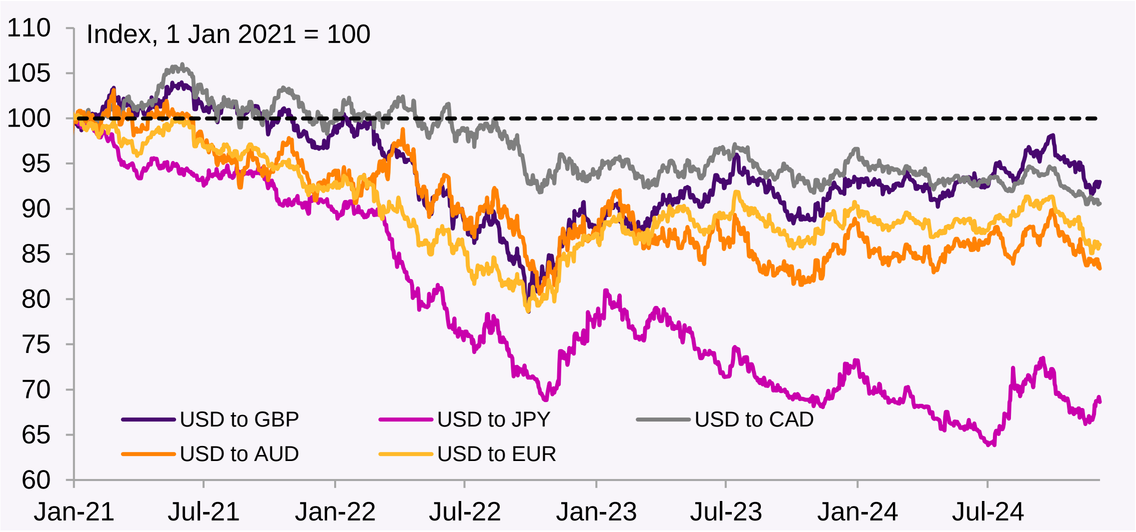
Factors influencing market trends:

Interest rate differentials help to explain these currency moves. The recent strengthening of the dollar has coincided with US Treasury yields rising relative to most other bond markets, helping to draw in capital. Since the beginning of November, 2-year interest rates have risen in the US relative to most other countries, particularly the Euro area, with Japan the notable exception. **Other factors also play a key role**. Growth and innovation have been better in the US than other markets, attracting investment and supporting the currency. **Over a three-year period, the US dollar has appreciated versus all major advanced economy currencies, particularly the yen.**

Looking ahead:

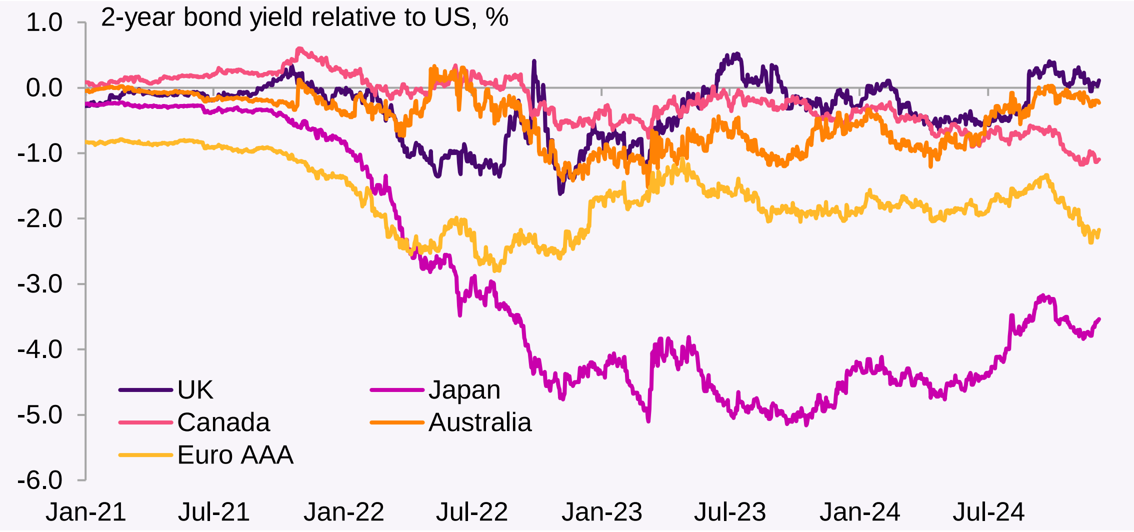
Following a sustained period of appreciation, the US dollar has become more expensive and less competitive against other major currencies on our preferred medium-term fair value metrics. This suggests downward pressure over a 3-to-5-year horizon and **a positive view on most developed market currencies against the dollar**. In the near term, however, the relative strength of the US economy, its safe-haven status, and the potential for additional trade tariffs by president-elect Trump could lead to further appreciation. In the shorter term, we are neutral on most currencies except for a positive view on the Japanese yen.

Developed exchange rates versus the US dollar



Sources: LSEG Datastream, WTW

Short term exchange rate dynamics have been influenced by differences in interest rates between countries



Sources: LSEG Datastream, WTW

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