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KEY INVESTMENT THEMES TO WATCH IN 2025

December saw a somewhat bumpy end to an otherwise stellar year for both local and global equity markets.

Global developed market equities (measured by the MSCI World Index) returned 19.2% in USD over the course of 2024, while their emerging market counterparts (MSCI Emerging Market Index) ended the year with a very respectable return of 8.1%, also in USD. In both cases, global developed and emerging markets returned nearly double their long-term average annual return; providing exceptional returns for investors with exposure to global markets.

Locally, our equity market (measured by the FTSE/JSE All Share Index) grew by 13.4% in ZAR, while our local bond market (FTSE/JSE All Bond Index) returned a whopping 17.2% to investors over the course of 2024. Investors who stayed the course and remained invested were well rewarded for their patience and would have generated returns well ahead of cash.

Despite a bout of December weakness on the back of dollar strength, our local currency also experienced a year of relative strength, ending the year among the five best-performing emerging market currencies. The last time the rand was a top-five performing emerging market currency was back in 2016.

Looking forward, inflation, interest rates, and the impact of Trump 2.0 remain the key areas of focus for markets in 2025. Below we have outlined key market themes for 2025 and how these factors can be expected to influence the different asset classes over the next 12 months, and where we continue to see opportunities for investment portfolios.

EQUITY MARKETS: MORE FUEL IN THE TANK?

Global risk assets are positioned for continued expansion heading into early 2025, supported by continued global economic growth and accommodative monetary policies. President Trump's pro-growth agenda in the US, including potential tax cuts and deregulation, reinforces the risk-on sentiment in the short term, building on the momentum of an already robust economy. However, despite a generally supportive global growth environment, global balanced portfolio returns are expected to moderate in 2025 following the exceptional performance of 2024. US and global equities, particularly in the US, face heightened risks of corrections due to high valuations and lofty earnings expectations.

Beyond the US, the global economic expansion is anticipated to broaden, with non-US markets gaining momentum. These regions are benefiting from improving earnings prospects and comparatively attractive valuations, offering a more favorable setup for the year ahead.

After entering 2024 with valuations close to historic lows relative to history for domestically focused companies in particular, local South African equities were priced to take advantage of any positive change in sentiment or underlying fundamentals. The National and Provincial Elections in May proved to be a turning point, with the formation of a Government of National Unity (GNU) exceeding expectations and sparking a significant recovery in SA Inc. stocks.

Looking ahead to 2025, many South African companies' valuations have returned closer to their long-term averages following the post-GNU rally. Optimism has been driven by expectations of reduced loadshedding, improved sentiment following the GNU's formation, and a lower interest rate environment driven by declining inflationary forces. However, corporate commentary in recent weeks suggests a mixed picture regarding the materialisation of these tailwinds. Despite this, the overall outlook remains cautiously optimistic.

ECONOMIC NEWSLETTER

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GEOPOLITICS

The anticipation of the Trump 2.0 era can hardly be understated, with his views surrounding tariffs, immigration, Tax cuts, and the ongoing war in Ukraine at the forefront of his proposed policies. Much of Trump's tariff rhetoric is seen as a negotiating tactic, unlikely to undermine US economic growth. This assumes that tariffs will be implemented selectively, resulting in only a modest increase in the overall US tariff rate. However, the possibility of a more disruptive scenario cannot be dismissed, and policy-related uncertainty and market volatility are likely to persist in the meantime.

Absent extreme policy measures, the baseline expectation is that strong economic fundamentals and robust growth momentum will drive the U.S. economy to another year of above-potential performance in 2025. A greater risk lies in the potential for higher-than-expected inflation, driven by possible policy shocks and an economy operating near full capacity.

LOCAL FIXED INCOME MARKETS CONTINUE TO SHOW VALUE

Globally, investors are likely to adjust their expectations upward for underlying inflation and long-term neutral policy rates. These shifts, along with expanding government budget deficits and elevated policy uncertainty, are expected to exert upward pressure on bond yields.

The expectation that the U.S. and G7 10-year government bond yields will trend higher next year warrants a relative underweight stance on duration with a preference for shorter-duration fixed income instruments. Although both the U.S. 2-year and 10-year Treasury bonds delivered modest positive returns this year, the 10-year has shown significantly greater volatility—a pattern expected to persist in 2025. Overall, maintaining an underweight stance on duration is justified across most G7 markets.

By comparison, our local South African Bond market continues to offer very attractive real yields to investors, with our 10yr Government Bond Index yielding investors real returns (after inflation) in excess of 6.0%.

CURRENCY TAILWINDS REMAIN IN PLACE

In a recent Analytics Exchange article we highlighted three primary SA-specific factors that appear to be driving the rand's outperformance relative to its Emerging Market counterparts, namely; improving economic sentiment post the GNU's reform implementation, a material reduction in SA's inflation rate resulting in high real rates earned by foreign investors, and positive seasonality factors driven by the holiday season.

Taking the above factors into account, it seems fair to argue that the Rand is unlikely to experience a bout of extreme sustained weakness in the near term.

The bottom line for 2025: Investors can expect ongoing volatility and dispersion of returns across markets and asset classes, however this will bring with it the opportunity to earn excess alpha. A sound investment process will be key to harnessing these opportunities and reaching your investment goals.