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With Profits Growth Fund Q4 2024 Review

WESLEYAN

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Market Review and Outlook

Markets surge following US election and rate cuts

It has been a positive quarter overall for global equities, with US stocks reaching record highs, bolstered by Donald Trump's election win. The global economy has proved to be surprisingly resilient, but inflation in some economies is now rising, putting central banks under pressure.

In this update, we'll reflect on this and take a look at some of the highlights, and the lowlights of the quarter – as well as bring our usual funds' view and outlook from our investments team.

Global market overview

The quarter began on a positive note, with tech sector gains and upbeat economic data boosting Wall Street. US share prices hit record highs after Donald Trump won the 2024 presidential election, despite his pledge to impose sweeping tariffs that could disrupt global trade. Major indexes rose and the dollar posted its biggest gain in eight years in response to Trump's proposed sweeping tax cuts and deregulatory policies.

Global bond yields saw their biggest rise in months in October as markets adjusted their outlook on interest rates. Strong data on consumer spending, job growth and inflation reduced hopes for swift rate cuts, pushing US Treasury yields higher.

In China, a brief stock market rally in early October faded after a key economic announcement fell short of investor hopes. Asian stocks were briefly unsettled by South Korean President Yoon Suk Yeol's declaration of martial law, although markets quickly recovered when the decision was reversed. Korea's won currency steadied but remained close to its two-year low against the dollar after being buoyed by suspected central bank intervention.

The FTSE 100 slipped following the first Budget from Labour Chancellor Rachel Reeves, while UK government bond yields pushed higher, reaching a one-year high. Meanwhile, European markets fell, weighed down by Russia-Ukraine tensions.

European stocks also came under pressure from political turmoil in France and Germany as the euro lost ground against other major currencies.

Gold hit an all-time high, driven by geopolitical tensions and central bank rate cuts. Oil prices fell below \$70 per barrel, prompting OPEC+ to postpone planned production increases.

Central banks balance rates and inflation

The US Federal Reserve delivered its third interest rate cut this year in December but warned that the pace of cuts is likely to be slower in 2025 as policymakers grapple with sticky inflation. US inflation fell to a three-and-a-half year low in September at 2.4%. It then ticked up in October to 2.6% and again in November to 2.7%.

The Bank of England cut interest rates for the second time this year in November. It set the rate at 4.75%, down a quarter percentage point from 5%, which is the lowest in more than a year. UK inflation dropped to 1.7% in September, its lowest level in three-and-a-half years and below the Bank of England's 2% target for the first time since 2021. However, a rise in energy bills helped push inflation up to 2.6% in November, its highest level in more than six months.

The European Central Bank (ECB) cut its key interest rate by a quarter percentage point to 3% in December – its fourth cut in

2024. Euro area inflation rebounded to 2.2% in November, up from 2% the previous month.

The US is now set to sharply diverge from Europe on monetary policy, as a divide between inflation and growth opens up between them. With higher growth and inflation, the Federal Reserve is likely to ease rates more cautiously. Meanwhile, the ECB is set for deeper cuts as growth slows and inflation falls.

US economy remains strong

The US economy is beginning to show signs of slowing but remains robust. The labour market rebounded in November from weak growth in the previous month, when hurricanes and strikes dampened hiring. Meanwhile, the unemployment rate has been rising for about a year, though it remains historically low. The underlying resilience of the economy suggests interest rates may remain higher for longer, with fewer cuts than initially expected. The election has fuelled optimism about domestic growth and inflation. While Trump's tax cuts are expected to support economic growth, proposed tariffs on imported goods could lead to higher prices.

Europe's economy grew at its fastest rate in two years during the third quarter, driven by stronger-than-expected growth in Germany and France. However, overall momentum remains weak. In a sign of deepening problems, Volkswagen, the country's largest industrial employer, has made significant job cuts and closed factories. The ongoing fallout from Russia's war in Ukraine and political upheaval in France and Germany has added to the pressure.

UK growth showed no growth in the third quarter, with uncertainty over the Budget being blamed for the lack of momentum. The UK's job market showed further signs of cooling after a rise in

unemployment, while pay growth slowed. The Labour government unveiled £40 billion of tax rises and ramped up borrowing to boost spending on public services in its first Budget in 14 years. However, business leaders have warned that tax increases in the Budget, including a rise in the national minimum wage and employers' National Insurance contributions could lead to job cuts.

The Chinese economy is also struggling to return to pre-pandemic levels of growth. Authorities are ramping up efforts to boost demand with additional stimulus to meet the 5% growth target for the year. However, economists believe it won't solve the deeper issues in the economy, such as a property slump, weak consumer spending and high unemployment, which continue to hinder recovery. There has also been a slowdown in export growth amid rising trade tensions with the US and European Union.

What this means for Wesleyan: our funds view and outlook

Investment markets wasted no time in reacting to the news of the sheer amount of UK Government Bonds (gilts) needed to prop up the Chancellor's growth plan for the UK economy. Unsurprisingly, the price of gilts dropped, making it more expensive for the government to borrow from investors as the yields on those gilts moved higher – 10-year gilt yields rose at the time to their highest rate in a year.

As long-term investors, we bought longer-dated gilts earlier this year, and, despite this recent rise, we still believe there is good long-term value in UK government bonds. This is something we will be looking at again in 2025 – particularly if yields move up closer to 5%. We also expect to continue making (selective) purchases of

corporate bonds, whilst being mindful of the extra risks that are associated with these if economies and companies begin to struggle.

We know that inflation and interest rates go hand in hand, but it's the outlook, rather than the current rate of inflation, that tends to sway central bankers, and this helps to explain why the ECB felt able to reduce interest rates for the third meeting in a row in December, but not the Bank of England.

The ECB were likely more concerned about weakening economic growth, whereas the Bank of England perhaps needs more reassurance that wage inflation is beginning to cool in the UK. The Bank of England's Monetary Policy Committee (MPC) voted to keep UK interest rates at 4.75% in December – with a view that marginal cuts would come in 2025.

We should keep some perspective on inflation – most countries globally are hovering around their 'target' inflation more so than they have been in a long while. However, there is one factor that could change all of that in the year ahead, and that is President-elect Donald Trump's highly publicised 'trade tariffs'. When he takes office in January 2025, the threat of him imposing them on countries such as China, Mexico, and Canada, amongst others, could become a reality.

At the start of the year, our Property Team set their own 'target', with ambitions to grow our commercial property portfolio with more than £100m of additional purchases. This was to compliment the circa £400m of properties we already held at the time. By the year end, the team had purchased almost £80m of additional assets, and they will continue with this plan (and potentially buy even more) during 2025. We had slowed down our purchases in the fourth quarter as we digested the budget impact (as mentioned

earlier). These assets form a core part of the expected long-term returns we'll be able to generate for our flagship With Profits Fund.

Our focus in 2025 will also be to continue to look at overseas equities, and we have made great progress on this in the last year. We have reduced our exposure to the UK within our mixed asset funds (including our With Profits Fund) during 2024, and this strategy will carry forward into the new year.

We continue to view UK equities as offering excellent long-term returns but also acknowledge that the UK stock market is a much smaller part of the investment world following strong growth in markets like America. We have always believed that diversification is important when riding out market turbulence and this could prove helpful in the year ahead.

INVESTMENT TEAM OF THE YEAR 2023

Our Investments team aim to outperform the markets over time to achieve strong returns to help investors reach their long-term financials goals. In recognition of their work, they were named 'Investment Team of the Year – re/insurer' at the Insurance Asset Risk Awards 2023, which recognises firms across the UK and Europe.



Please note that past performance is not a reliable guide to future performance and the value of your investment, and any income can go down as well as up, so you could get back less than you invested.

If you have any queries or would like more detail about Wesleyan's With Profits Growth Fund please speak to your adviser.

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