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Investment Commentary

Q1 2025

Overview

Financial markets loathe uncertainty, and they have had to contend with a bucket load of it over the past three months. Concern was heightened before Donald Trump's inauguration as the 47th President of the United States. His threats to global trade, with the use of tariffs, to geopolitics, through the near-abandonment of NATO and his interventions in Ukraine and Gaza, and to workforces in the US, with forced immigrant expulsion, all caused volatility in markets. One day tariffs were levied on Canada and Mexico, and the next they were not. Interpreting such policy, if it is such a thing, is nearly impossible – and events since the end of the quarter have worsened further.

While rapidly becoming irrelevant, what did happen over the first quarter? The US economy continued its resilient performance, having expanded by 2.4% in the fourth quarter of 2024. Employment numbers remained strong, despite federal cutbacks and some immigrant deportations. Inflation remained higher than target, at around 3.0%, and both the services and manufacturing PMIs remained above 50 – the measure of expansion. In reaction to this, the Federal Reserve Bank saw fit to leave interest rates unchanged, at 4.5%.

The UK economy defied expectations by growing 0.1% in the fourth quarter. The services sector PMI remained in growth territory, at 52.4, while the manufacturing reading fell to 44.9 in March. The Bank of England cut interest rates by to 4.5% – a reduction of 0.25% – while inflation, at 2.8%, remained stubbornly above target. At +5.8% year on year in January, wage growth remains strong and will increase further as the minimum wage increases take effect in April. Yet the government's flagship housebuilding policy already looks unachievable. Stamp duty thresholds are being cut, "Help to Buy" is coming to an end, and owners of rental properties are selling up as policy turns against them. The construction PMI reading was 46.4 in March.

In Europe, meanwhile, political change, especially in Germany, has been significant. Trump's insistence that European countries spend more on defence, alongside weak economic growth in general, has driven action. Germany has voted to lift a longstanding fiscal straitjacket, leading to a huge proposed stimulus over the next 10 years. Spending on defence and infrastructure combined will amount to over €1tn. In the eurozone the services PMI continues to show the sector expanding, but, as elsewhere, manufacturing is still contracting. Inflation has remained closer to target, at 2.2%, and the European Central Bank has cut rates by 0.5%, to 2.65%, over the quarter.

China, one of the main targets for Trump's tariffs, saw its economy grow by 1.6% in the fourth quarter of 2024. Both services and manufacturing expanded, according to PMI numbers. India's economy, recovering from a slowdown in the middle of last year, grew by 1.6% in the last quarter of 2024.

The following table sets out the market movements for the first quarter.

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Index	31/12/2024	31/03/2025	Q1 Change
CBOE UK 100	819	856	4.5%
CBOE UK All Companies	14,355	14,849	3.4%
CBOE UK 250	18,057	16,962	-6.1%
MSCI Private Balanced	1,936	1,908	-1.4%
MSCI Private Growth	2,222	2,178	-2.0%

Markets

The UK market performed relatively well over the three months to 31st March but was again driven by the largest companies. The oil sector was up 12%, with BP (+11%) and Shell (+14%) significant contributors. The bank sector (+14%) also pulled the main index higher, with Lloyds leading (+32%) and others up by double-digit percentages. Financials generally did well, with many insurance names outperforming. On the negative side, retailers, house builders and industrial companies all experienced weakness.

While the main index was up, the next 250 stocks, smaller companies and AIM indices all fell by around 5%. We have continued to see takeover activity in these areas of the market as value is increasingly recognised. Regrettably, events in the first few days of April have seen all the quarterly gains – and more – wiped out, as the main index has corrected by some 10% from its early-March highs.

As we have repeatedly reported, the largest technology stocks in the US have driven market indices higher. The S&P 500 reached an all-time high on 19th February, since when it has pulled back by some 18% (at the time of writing). The most newsworthy stocks from last year have seen some of the steepest falls, with Nvidia down 22% and Tesla down 37% over the quarter.

The stimulus proposed by the German government-in-waiting drove the market to a record high in mid-March and up 11% over the quarter. However, as elsewhere, much of this gain has been given back in recent days.

China's promise of stimulus drove its stock market higher in early October, and it has managed to hold on to much of this gain so far. The Indian market, in contrast, has been steadily sliding since last September and was down 4.5% over the quarter. Having been a strong performer in 2024, Japan fell 11% in the first quarter as inflation rose and trade was threatened.

Outlook

Trump's extraordinary decision to place tariffs on trade with most countries around the world has caused significant turmoil in financial markets. China's retaliatory tariffs on American goods make it look as if a trade war is coming. Other countries are considering their responses, but the expectation that this may lead to higher inflation and ultimately recession has been taken to heart. Only time will tell if Trump's move will turn out to be part of a negotiating tactic or a long-term (and probably highly negative) step for the global economy.

The knee-jerk reaction by equity markets, which have fallen by between 5% and 10% this month (April), is obviously hard to absorb. It may prove to be an overreaction. Timing markets is notoriously difficult. For long-term investors it is time in the market, not market timing, that delivers the best long-term returns. We advocate holding one's nerve and sticking with investments in quality companies while we ride out the current storm.

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