MARKETING MATERIAL

Quarterly CIO View | Letter to Investors
Client audience Retail

DWS

November 21, 2024

2025: continuation amid disruptions

In 2025 growth and inflation trends that are returning to normal meet a U.S. president who wants to turn things upside down. But the unpredictability may not be all bad and, as far as we can see today, the year could in fact turn out well for investors.

Vincenzo Vedda
Chief Investment Officer

> "We expect 2025 to be a good year for investors overall, as inflation eases, growth returns to normal and central bank interest rate cuts help many asset classes. However, stock valuations leave little room for negative surprises and, after the U.S. presidential election, we should expect the year to be anything but predictable. Our approach is to be ready for anything."

These are exciting times in which to take up the position of Chief Investment Officer at DWS, where I have been working since 2013. 'Exciting', you know, is a euphemism for challenging. We are heading into 2025 as thoroughly pampered investors. Global equities have gained over a fifth during the current year so far. Since their low in autumn 2022, they have gained almost two-fifths. Gold and silver have become a quarter more expensive in 2024 and corporate bonds have also done well. What more could we hope for next year? – especially given that we do not expect any pick-up in global economic growth, with 3.1% GDP growth being our expectation this year and in 2025 and 2026. U.S. equities, meanwhile, are already so highly valued that their risk premium is negative for the first time in over 20 years. In the case of (U.S.) bonds, the downward trend in yields, especially at the longer end, was already broken in September and completely reversed with Donald Trump's re-election. How then can next year nonetheless be good for investors? I will explain.

The new U.S. president does not want 'business as usual' – the unexpected is on the agenda

One of the biggest challenges for the coming year is certainly how to deal with the new, old president of the U.S. Yes, the stock markets in particular were quick to celebrate his re-election. However, there can be little doubt that Trump will not be able to implement all of his plans in full, especially since some of them counteract one another. For example, getting a grip on the cost of living crisis, i.e. lowering inflation faster, is unlikely to go hand in hand with import tariffs and a ban on migration. In addition, his unconventional approach to office could unsettle some economic players (especially foreign ones) and increase volatility in some market segments. However, volatility – although undesirable for most investors – can involve both positive and negative swings.

Positive economic core scenario – good conditions for many asset classes

The positive aspects for the 2025 investment year drive our core economic scenario. The global economy is continuing to approach normality in terms of growth, inflation, which has fallen substantially, and interest rates. We do not expect a recession in any of the major economies, but rather steady, moderate growth. This is a very good environment for many asset classes. Stock markets rarely slide into a bear market without a pronounced slump in GDP. Equities should continue to be driven primarily by rising earnings, which we expect on both sides of the Atlantic. However, in the U.S., this growth is likely to continue to be strongly driven by the large tech stocks, which we expect will therefore retain their dominant position in the stock markets. In order to avoid being fully exposed to the resulting concentration risk we have no regional preferences and we foresee high single-digit returns on average globally for equities by the end of 2025. However, we believe investors should prepare themselves in good time for the fact that equities are more likely to see mid-single-digit total returns in coming years, not least due to the currently high valuation multiples.

In the bond market we expect yield curves to steepen further in 2025 as central banks' interest rate cuts leave their mark on two-year bond yields in particular. At the end of 2025 we see the Fed Funds rate at 3.75-4.00% and the ECB deposit rate at 2.0%. Corporate bonds should remain attractive in 2025 due to their high current interest yield and overall robust economy. However, we do not expect yield spreads to narrow further. We prefer bonds with investment grade status to those without.

Alternative assets are enjoying little tailwind from monetary policy due to fairly stable interest rates at the long end, but fundamental conditions are improving in many areas, for example in residential real estate.

We do not expect gold to rally as it did in 2024, but we expect it will still achieve a decent gain. In any case, we believe that the precious metal is likely to serve as a good hedge in a challenging year 2025. Why? Well, even though our core scenario is positive for 2025, this time the range of threats to this scenario is far larger than usual. We believe a wide range of developments are possible. Much depends on how the current geopolitical flashpoints (Ukraine, Middle East, Taiwan potentially) develop; the patience of the bond markets in the face of the unchecked U.S. debt binge; the extent of further AI investment euphoria and, of course, the decisions that the presumably unconventional next U.S. administration will take. The unpredictability may not be entirely bad; it cannot be ruled out that changes initiated by the U.S. could lead to some fresh positive momentum on some currently deadlocked issues. Broad diversification across different asset classes, styles and maturities should help to minimize the impact of individual risks.

[1] Calculated as the earnings yield of equities (current earnings per share divided by the share price) minus the 10-year government bond yield.

This information is subject to change at any time, based upon economic, market and other considerations and should not be construed as a recommendation. Past performance is not indicative of future returns. Forecasts are based on assumptions, estimates, opinions and hypothetical models that may prove to be incorrect. Alternative investments may be speculative and involve significant risks including illiquidity, heightened potential for loss and lack of transparency. Alternatives are not suitable for all clients.

Glossary

Artificial intelligence is the theory and development of computer systems able to perform tasks normally requiring human intelligence.

Technically, a bear market refers to a situation where the index's value falls at least 20% from a recent high.

The deposit rate is the rate banks receive when they make overnight deposits with the ECB.

Diversification refers to the dispersal of investments across asset types, geographies and so on with the aim of reducing risk or boosting risk-adjusted returns.

The federal funds rate is the interest rate, set by the Fed, at which banks lend money to each other, usually on an overnight basis.

The gross domestic product (GDP) is the monetary value of all the finished goods and services produced within a country's borders in a specific time period.

Inflation is the rate at which the general level of prices for goods and services is rising and, subsequently, purchasing power is falling.

Investment grade (IG) refers to a credit rating from a rating agency that indicates that a bond has a relatively low risk of default.

A recession is, technically, when an economy contracts for two successive quarters but is often used in a looser way to indicate declining output.

The risk premium is the expected return on an investment minus the return that would be earned on a risk-free investment.

The spread is the difference between the quoted rates of return on two different investments, usually of different credit quality.

A tariff is a tax imposed by one country on the goods and services imported from another country.

Volatility is the degree of variation of a trading-price series over time. It can be used as a measure of an asset's risk.

Yield is the income return on an investment referring to the interest or dividends received from a security and is usually expressed annually as a percentage based on the investment's cost, its current market value or its face value.

Important information

DWS is the brand name of DWS Group GmbH & Co. KGaA and its subsidiaries under which they do business. The DWS legal entities offering products or services are specified in the relevant documentation. DWS, through DWS Group GmbH & Co. KGaA, its affiliated companies and its officers and employees (collectively "DWS") are communicating this document in good faith and on the following basis.

This document is for information/discussion purposes only and does not constitute an offer, recommendation or solicitation to conclude a transaction and should not be treated as investment advice.

This document is intended to be a marketing communication, not a financial analysis. Accordingly, it may not comply with legal obligations requiring the impartiality of financial analysis or prohibiting trading prior to the publication of a financial analysis.

This document contains forward looking statements. Forward looking statements include, but are not limited to assumptions, estimates, projections, opinions, models and hypothetical performance analysis. No representation or warranty is made by DWS as to the reasonableness or completeness of such forward looking statements. Past performance is no guarantee of future results.

The information contained in this document is obtained from sources believed to be reliable. DWS does not guarantee the accuracy, completeness or fairness of such information. All third party data is copyrighted by and proprietary to the provider. DWS has no obligation to update, modify or amend this document or to otherwise notify the recipient in the event that any matter stated herein, or any opinion, projection, forecast or estimate set forth herein, changes or subsequently becomes inaccurate.

Investments are subject to various risks. Detailed information on risks is contained in the relevant offering documents.

No liability for any error or omission is accepted by DWS. Opinions and estimates may be changed without notice and involve a number of assumptions which may not prove valid.

DWS does not give taxation or legal advice.

This document may not be reproduced or circulated without DWS's written authority.

This document is not directed to, or intended for distribution to or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, including the United States, where such distribution, publication, availability or use would be contrary to law or regulation or which would subject DWS to any registration or licensing requirement within such jurisdiction not currently met within such jurisdiction. Persons into whose possession this document may come are required to inform themselves of, and to observe, such restrictions.

© 2024 DWS Investment GmbH

Issued in the UK by DWS Investments UK Limited which is authorised and regulated in the UK by the Financial Conduct Authority.

© 2024 DWS Investments UK Limited

In Hong Kong, this document is issued by DWS Investments Hong Kong Limited. The content of this document has not been reviewed by the Securities and Futures Commission.

© 2024 DWS Investments Hong Kong Limited

In Singapore, this document is issued by DWS Investments Singapore Limited. The content of this document has not been reviewed by the Monetary Authority of Singapore.

© 2024 DWS Investments Singapore Limited

In Australia, this document is issued by DWS Investments Australia Limited (ABN: 52 074 599 401) (AFSL 499640). The content of this document has not been reviewed by the Australian Securities and Investments Commission.

© 2024 DWS Investments Australia Limited

For institutional / professional investors in Taiwan:

This document is distributed to professional investors only and not others. Investing involves risk. The value of an investment and the income from it will fluctuate and investors may not get back the principal invested. Past performance is not indicative of future performance. This is a marketing communication. It is for informational purposes only. This document does not constitute investment advice or a recommendation to buy, sell or hold any security and shall not be deemed an offer to sell or a solicitation of an offer to buy any security. The views and opinions expressed herein, which are subject to change without notice, are those of the issuer or its affiliated companies at the time of publication. Certain data used are derived from various sources believed to be reliable, but the accuracy or completeness of the data is not guaranteed and no liability is assumed for any direct or consequential losses arising from their use. The duplication, publication, extraction or transmission of the contents, irrespective of the form, is not permitted.

as of 11/19/24; RBA 0087 / CRC 102646_2 (11/2024)