

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.

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

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.

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as of 11/19/24; CRC 102647_2 (11/2024)