HORIZON

The Berenberg Capital Market Outlook · Wealth and Asset Management

RATES TURNAROUND HELPS

The looser monetary and fiscal policy worldwide should support the economy and allow the markets to continue to count on a favourable economic environment. The risks lie in US trade and foreign policy, as well as in the development of inflation and national debt. The further rate path and the Fed's policy are therefore subject to a high degree of uncertainty.

REALLOCATION FORWARD

In 2024, investors have again put a lot of money into short-term interest-bearing investments such as money market funds and time deposits, but interest rates are falling. In 2025, they could turn to other investments and gold, corporate bonds and equities could benefit.

A TOUGHER BULL MARKET

With positive earnings growth and more corporate takeovers, the stock markets still have some potential. However, given the political risks, setbacks and higher volatility are likely, as valuations are high and investor sentiment and positioning are optimistic.

Q1 | 2025

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FOREWORD

Prof Dr Bernd Meyer
Chief Investment Strategist

Dear readers,
"Challenging, but with opportunities" was the title of our outlook for 2024. In the first half of the year, the changing market narrative between fears of excessively strong and excessively weak US growth, the resulting sharp fluctuations in bond yields and the low market breadth proved particularly challenging. Throughout the year, markets wrestled with the question of whether the US economy would achieve a soft landing. Ultimately, economic performance in 2024 was better than expected in many regions, especially in the US, and 10-year government bond yields rose despite central banks cutting interest rates. Investors were offered numerous opportunities. Gold, equities and industrial metals all posted double-digit gains. We had expected equity markets to reach new highs, but the extent surprised us. Almost all bond segments also posted gains, led by corporate and high-yield bonds. Investors who relied on short-term interest-bearing investments such as time deposits were left behind.

What can investors expect in 2025? Lower inflation rates, falling central bank rates, especially in Europe, and likely new fiscal stimulus suggest a market-friendly economic environment, positive earnings growth and a continuation of the equity bull market. However, a lot of good news is already priced into US equities, investor sentiment and positioning are optimistic, and there is a high level of uncertainty regarding US trade and foreign policy and the US national debt under President Trump. The risks for the markets are by no means only to the downside, as for example the much-discussed tariffs, falling immigration or the increasing tensions between the US and China. For example, if the situation surrounding Russia's war in Ukraine and the conflict in the Middle East eases, energy prices should fall, central banks should lower interest rates more sharply and economies should perform better, particularly in Europe. US deregulation under President Trump, a new government in Germany or stronger fiscal policy measures in China could also provide positive impetus. An increase in corporate takeovers and a reallocation of investor funds from short-term interest-rate investments should also provide support.

We therefore expect the bull market in equities to continue, but that the third year will be more volatile and difficult, with more setbacks and less potential for equities. In particular, President Trump's inauguration could make investors more cautious. This is because the clear election result could be seen by him as a mandate to push through his policies quickly and without compromise, which could weigh on the capital markets, at least temporarily. Bonds are likely to produce only moderate gains in 2025, while gold will remain supported by increased uncertainty and central bank purchases. We are confident that broad multi-asset portfolios will continue to outperform short-term interest-rate investments by a wide margin in 2025 despite all the uncertainties and risks.

In the Insights interview starting on page 14, Vincent Kalmes, Head of Multi Asset Internal Advisory, talks about how investment ideas are developed and refined for the advisory business at Berenberg. All the best for 2025!

CONTENT

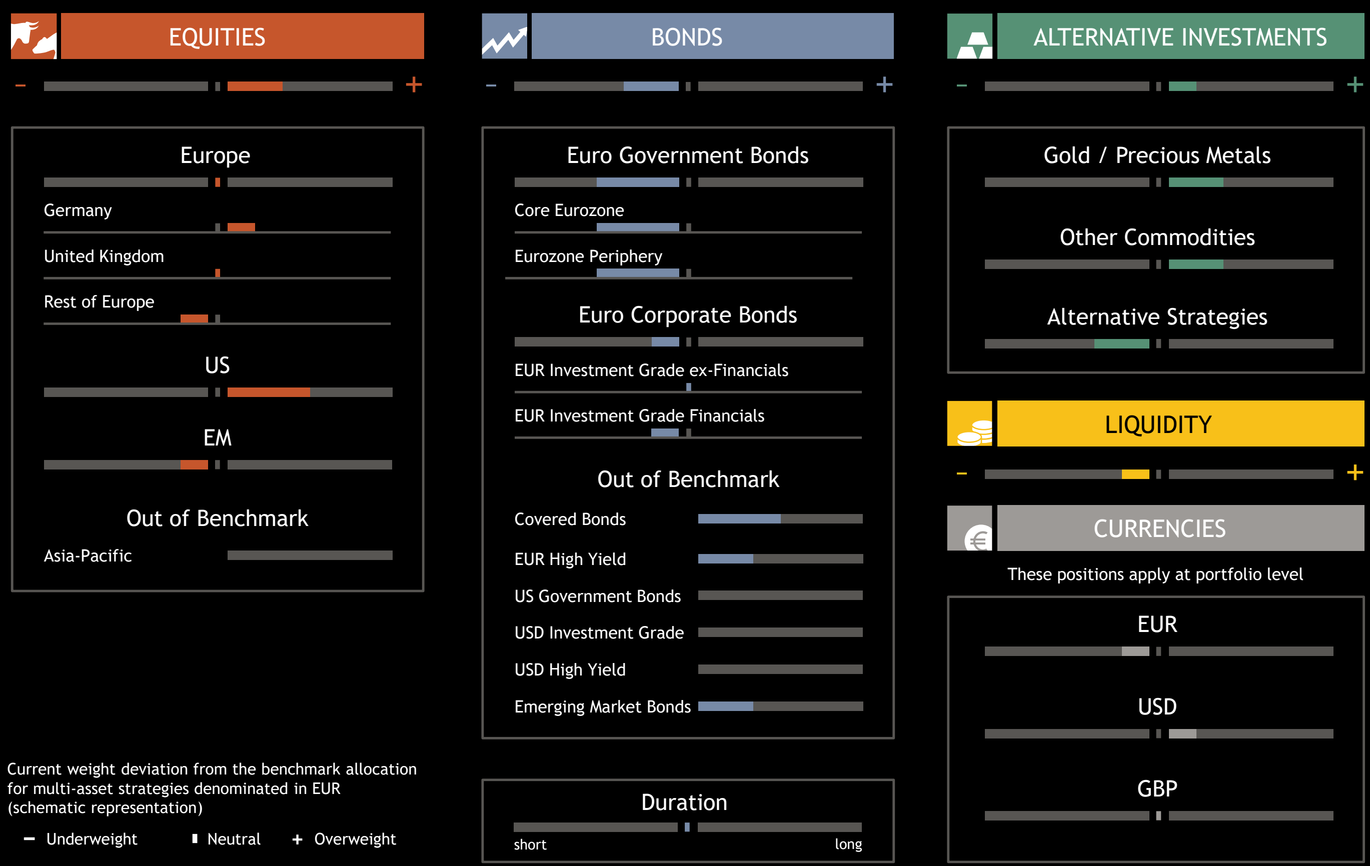
MORE VOLATILITY IN POLITICS AND FINANCIAL MARKETS

IN A NUTSHELL

- The economic environment, increasing corporate takeovers and a reallocation of investor funds from short-term interest-rate investments suggest that the bull market will continue.
- The numerous political risks, the high valuations of (US) equities and the low credit risk premiums on corporate bonds are limiting the return potential of risky investments. More setbacks and higher volatility are to be expected. Government bonds offer little potential.
- After the start of the year, at the latest with the swearing-in of Donald Trump on 20 January, things are likely to get tougher.
- The trend towards more market breadth from the second half of 2024 should continue in 2025 and support small cap stocks.

Portfolio positioning at a glance

In view of the uncertainty surrounding the US election outcome, we started the fourth quarter with a balanced positioning. An overweight in bonds or long duration was also not on the cards, as we considered the market's expectations of interest rate cuts to be exaggerated. With the increasing probability of a Trump victory, we built up our equity holdings further ahead of the election, particularly US mid caps, partly at the expense of Europe. We took a further step immediately after Trump's victory. As we enter the new year, we are sticking to our overweighting of (US) equities and commodities over bonds and cash, but expect markets to become more volatile again, at the latest from when Donald Trump is sworn in. Government bonds offer little potential in 2025 – unless there is an economic downturn or an escalation of geopolitical risks. Corporate bonds offer more attractive yields, but risk premiums are fair at best. We see opportunities in local currency bonds from emerging markets and in high-yield bonds. Gold has performed very well, but remains significantly overweighted. Other commodities, particularly industrial metals, remain a sensible portfolio addition due to their tangible value and are supported by structural trends.



Fourth-quarter review: Trump and positive economic signals

Economic surprises in the US, the eurozone and China turned positive as early as the beginning of October. The market's high expectations of interest rate cuts were subsequently corrected, and bond yields rose. Gold continued to rise, supported by steady inflows. Otherwise, as expected, much of the focus was on the US elections. The likelihood of a Trump victory increased during October and, following his landslide victory, left its mark on the markets. The US dollar and US equities, in particular small caps, rose significantly. Rising yields weighed on government bonds, while equities from the rest of the world stagnated. Corporate bonds, especially high-yield bonds, continued to be the top performers among bonds, and both oil and industrial metals rose significantly.

Positive economic outlook - but with a multitude of risks

Falling central bank interest rates worldwide, disinflation and further fiscal stimulus in the US and China should support the economy in 2025. Economists largely agree that the global economy will grow at a similarly strong rate in 2025 as in 2024. The consensus view is that the US economy will lose momentum due to cooling domestic demand and labour market conditions, while Europe is positioned for a slight recovery (top chart p. 5). Our economists paint a similar picture. Compared to a year ago, the risk of a hard landing of the US economy has decreased significantly. The existing Fed put, ie the possibility that the Fed could cut interest rates even further in an emergency, has recently been supplemented by a Trump put. Both support the prevailing market optimism.

In addition to US politics, the development of inflation and the US national debt are likely to be among the most important topics in 2025 and are subject to a high degree of uncertainty. With regard to US inflation, deregulation, lower energy prices, a stronger US dollar and the release of labour in the public sector could counteract the inflationary effect of tariffs and lower immigration. Here it is a matter of waiting and observing the situation, especially since Trump's starting position is much more difficult than in 2016, when the economy was close to deflation, equities were moderately valued, corporate profit margins were low, the tax burden was high and the budget deficit was low. In 2024, the economy is strong, the deficit is around 7% of GDP, profit margins are high, the tax burden is lower and US equity valuations are close to all-time highs. Trump's policies at this time – tariffs, tax cuts and immigration restrictions – are likely to have less of an impact today and entail greater risks. The future interest rate path and Fed policy are therefore subject to a high degree of uncertainty. This is likely to lead to higher volatility in the financial markets. A sharp rise in bond yields poses a major risk for highly valued (US) equities and corporate bonds, especially if inflation were to pick up again and the Fed were forced to tighten in the second half of the year – as it did in 2018.

Potential returns are likely to be more limited in 2025

The positive economic outlook, an increase in corporate takeovers and a possible reallocation of investor funds from short-term interest-rate investments (see below) suggest a continuation of the stock bull market that has been ongoing since October 2022.

US dollar and US equities benefited from Trump's victory in Q4, while European and EM equities suffered, along with government bonds.

Total return	YTD and in Q4 2024 (in %, in EUR)		12-month periods of the last 5 years (in %, in EUR)					CAGR*	Std.-dev.*
	YTD (31/12/23-09/12/24)	Q4TD (30/09/24-09/12/24)	09/12/23 09/12/24	09/12/22 09/12/23	09/12/21 09/12/22	09/12/20 09/12/21	09/12/19 09/12/20	09/12/19 09/12/24	09/12/19 09/12/24
Gold	34.9	6.5	35.2	9.4	8.4	3.2	15.3	13.8	14.0
S&P 500	34.6	11.1	35.7	16.7	-8.3	37.8	9.3	16.9	21.1
DAX	21.5	5.3	21.4	16.6	-8.1	17.2	1.8	9.2	20.4
MSCI EM	16.4	0.4	19.0	0.3	-13.6	8.5	11.8	4.6	17.2
EM Sovereigns	13.2	5.6	13.7	3.5	-9.5	6.8	-2.9	2.0	8.5
Stoxx Europe 50	11.2	-0.2	12.0	10.5	4.3	23.2	-4.3	8.7	16.6
Brent	10.0	7.7	8.7	7.4	41.5	79.4	-38.4	12.8	39.7
US Sovereigns	7.1	3.9	6.9	-2.0	-5.3	4.8	-1.5	0.5	7.0
EUR Corporates	5.4	1.6	7.3	3.8	-12.7	-0.6	2.8	-0.1	4.0
USDEUR	4.6	5.5	2.0	-2.1	7.1	7.0	-8.4	0.9	7.4
Euro Overnight Deposit	3.6	0.6	3.8	3.1	-0.2	-0.6	-0.5	1.1	0.1
EUR Sovereigns	3.3	0.9	4.9	1.4	-10.0	-1.0	2.0	-0.7	3.9

Time period: 09/12/2019-09/12/2024.
Source: Bloomberg * CAGR = annualised return (in %, in EUR); Std. dev. = annualised standard deviation (in %, in EUR).

Historically, bull markets last an average of six years. However, a repeat of the very good performance and low volatility of the last two years seems unlikely. The consensus forecast for US earnings growth in 2025 is in the double-digit percentage range, despite a decline in nominal growth and already record-high profit margins. A lot of optimism is already priced in and investor positioning is already pronounced, so the upside potential for US equities in particular appears more limited than it has been recently. Historically, the third year of a bull market in the US has tended to be weak, with the S&P 500 returning just 6%. For European equities, risks and risk premia are high, making performance highly dependent on the macroeconomic and political environment. Bonds are likely to produce only moderate gains, while gold should remain supported by increased uncertainty and central bank purchases.

2025: Support through reallocation from money market funds

In 2024, investors again "parked" a lot of money in short-term interest rate investments such as money market funds or time deposits. Even though they increasingly turned to equities and bonds, money market funds continued to have the highest inflows both in absolute terms and relative to their total assets. Over the last 12 months, holdings in US money market funds have risen by USD900bn to USD6.8trn. So far, this strategy has not paid off for investors – over the last 12 months, all other asset classes have outperformed (table p. 4). With the interest rate cuts, reinvestment is now becoming increasingly unattractive. As the economy strengthens, investors are likely to turn to other investments. In the past, money market funds have experienced outflows about 6-12 months after the first rate cuts (see chart below).

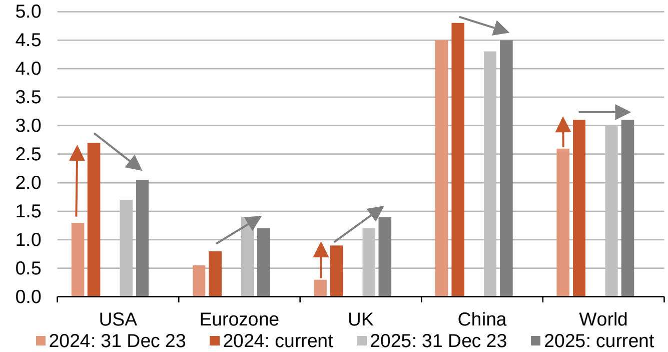
More demanding markets at the latest after Trump's swearing-in

Stocks should remain supported into the new year, not least due to positive seasonality. However, the implementation of Trump's policies could result in at least temporary pressures (middle chart). In addition, markets have developed certain expectations of an easing of the geopolitical situation, which could be disappointed. The recent deterioration in financial conditions in the US (stronger US dollar, higher bond yields) could become a headwind for the US economy, and US economic surprises in the first quarter could turn negative again.

Prof Dr Bernd Meyer, Chief Investment Strategist

2024 - better than expected; 2025 - US weaker, Europe stronger

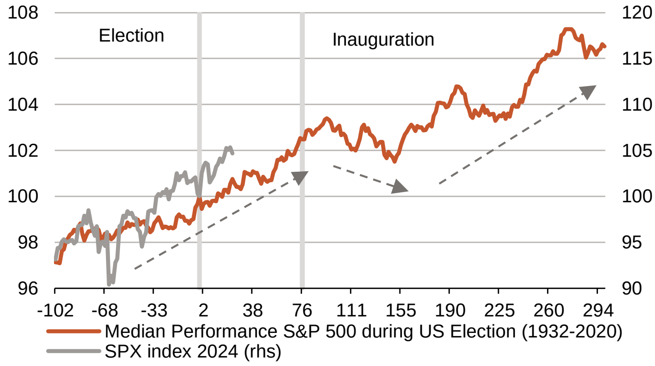
Real GDP growth expectations (economists consensus) for 2024 and 2025 a year ago and currently



Time period: 31/12/2023-09/12/2024
Source: Bloomberg, own calculations

A stock market rally without setbacks seems unlikely in 2025

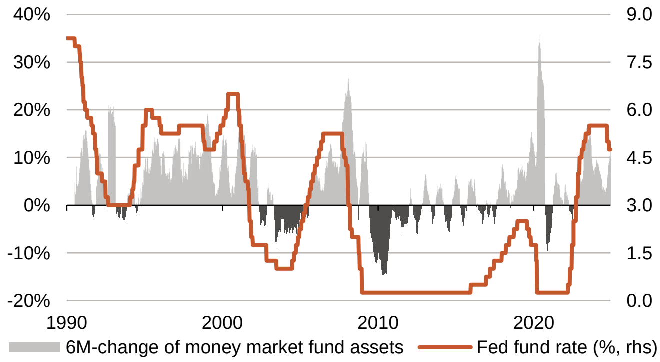
After a new US president takes office, there is often a breather in the stock markets.



Time period: 01/01/1932-09/12/2024
Source: Bloomberg, own calculations.

Money market fund outflows start about 12 months after rate cuts

6M changes in money market fund holdings (%) compared with the Fed funds rate



Time period: 01/01/1990-09/12/2024
Source: ICI Investment Company Institute, Bloomberg, own calculations

US CONTINUES TO OUTPACE EUROZONE ECONOMICALLY

IN A NUTSHELL

- US: Trump is back.
- Europe: Germany puts the brakes on the eurozone.
- Inflation: The last few metres are the hardest.
- Monetary policy: the easing is coming to an end.

US: Trump is back

The US economy remains very robust and is hardly losing any momentum. GDP growth in the third quarter was an annualised 2.8%, and thus again well above the trend growth rate of around 2.0%. The economy was driven by continued solid private consumption, exports and government spending. Although the labour market, which was still clearly overheated at the beginning of 2024, cooled noticeably over the course of the year, there was no slump. The unemployment rate has even fallen again recently and, at just over 4%, is still at a low level by historical standards. At present, therefore, it looks as if the US economy will experience a very soft landing. Re-elected US President Donald Trump could even provide further growth impetus in the coming year through tax cuts and deregulation. However, if he introduces high tariffs on imports from China and other countries, this would drive up prices in the US and fuel inflation. The fact that the affected countries would in all likelihood respond to US tariffs with countermeasures would also have a negative impact on the US economy. Trump is also planning to significantly tighten immigration policy. From an economic point of view, this would exacerbate the labour shortage that is already being felt in many areas. This would further drive up inflation and reduce US growth potential in the medium term. Overall, we therefore expect a certain economic boost for the US in the coming years as a result of Donald Trump's return, with GDP growth rates above the 2% mark. In the medium to long term, however, trend growth in the US is likely to suffer from the planned measures.

Political uncertainties in Germany and France

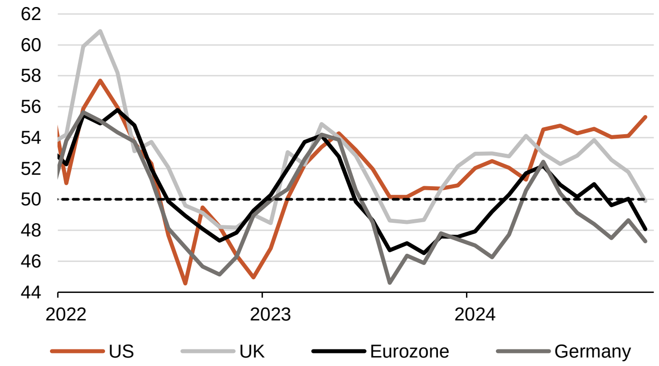
The eurozone economy was surprisingly able to grow by 0.4% in the third quarter compared to the previous quarter. Growth was once again very uneven. While the growth rate in Spain was 0.8%, the German economy was only able to grow by 0.1%. The leading economic indicators for the eurozone suggest that growth will slow towards the end of the year. Sentiment is particularly poor in the two largest economies in the eurozone, France and Germany. In both countries, political uncertainty is dampening economic development. While the future is wide open in France following the fall of the government, the coalition of the traffic light system in Germany has collapsed and new elections are scheduled for 23 February.

New elections in Germany open up opportunities for growth

The eurozone will only be able to get back into its stride once the largest member state returns to a growth path. The German economy has been treading water for three years now. There are many

Economic indicators in the US are significantly stronger than in Europe

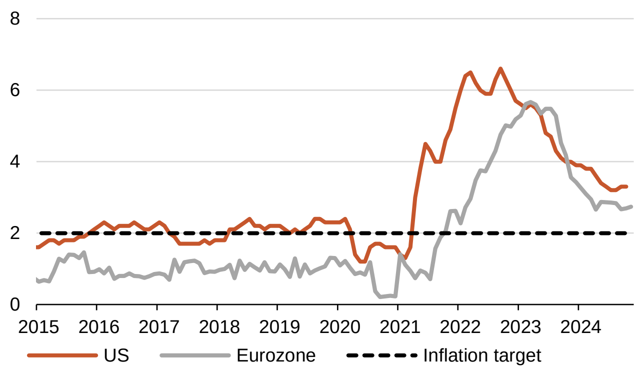
Purchasing Managers' Indices, overall index in index points, growth threshold = 50 points



Period: 01/2022–11/2024
Monthly data. Source: S&P Global

Core inflation has recently moved sideways

Year-on-year increase in consumer prices in %



Period: 01/2015–11/2024
Monthly data, core inflation. USA: CPI-U, Eurozone: HICP, Sources: BLS, Eurostat

reasons for this. On the one hand, global demand continues to weaken, which hits Germany particularly hard as an export nation. In addition, Chinese products are increasingly competing with German products in global markets. The labour shortage and excessive bureaucracy are also having a negative impact. The fact that the coalition government has spent more time arguing than implementing necessary reforms has paralysed the German economy in recent quarters. The new elections on 23 February 2025 therefore also offer the opportunity to end the political uncertainty and tackle overdue reforms. At present, there are many indications that a grand coalition will be re-established. In the coalition negotiations, the SPD could possibly wrest a reform of the debt brake from the CDU in order to create scope for urgently needed public investment and additional defence spending. In return, the SPD would then have to make concessions on economic and social reforms. All in all, a package could be put together that would give the German economy a slight tailwind.

Cautiously optimistic outlook for Germany and the eurozone

A number of factors, including the recovery of the German economy, suggest that the eurozone economy will pick up in the coming year. Consumer spending is likely to increase due to the fact that wages have been rising faster than prices for some time. In addition, the measures taken by China to support its economy and the growth impulses triggered by Trump in the US will boost foreign demand. The recent depreciation of the euro against the US dollar will also have a positive effect on exports. In addition, the interest rate level, which is likely to fall further in the coming months and thus make investments more attractive for companies again, is also contributing to the cautiously positive outlook. A ceasefire in Ukraine would further improve sentiment. By contrast, the biggest risk for the economy in the euro area comes from possible US tariffs.

The last few metres are always the hardest for central banks

The significant decline in inflation rates enabled the Fed and the ECB to start lowering key interest rates in 2024. However, they have recently made little progress on both sides of the Atlantic in combating core inflation excluding energy and food. The ECB will therefore only support the economy in the eurozone with small interest rate cuts of 25 basis points. We expect three further steps and foresee the deposit rate at 2.25% at the end of Q2 2025. In the US, by contrast, Donald Trump's return to the White House has significantly complicated the situation for the Fed. This is because Trump's plans to loosen fiscal policy, impose extensive tariffs and severely restrict immigration would, if implemented, drive up inflation. This would likely force the Fed to lower key rates more cautiously and by less than we had previously expected. We therefore now expect the Fed to lower key rates only once in the first quarter of 2025, leaving the key interest rate range at 4.25% to 4.50%.

Dr Felix Schmidt, Senior Economist

Growth and inflation forecasts

	GDP growth (in %)						Inflation (in %)					
	2024		2025		2026		2024		2025		2026	
		∅**		∅**		∅**		∅**		∅**		∅**
USA	2.8	2.7	2.4	2.1	2.2	2.0	3.0	2.9	2.9	2.4	2.6	2.5
Eurozone	0.7	0.8	1.0	1.1	1.5	1.2	2.4	2.4	2.0	2.0	2.2	2.0
Germany	-0.2	-0.1	0.3	0.6	1.2	1.2	2.5	2.4	2.1	2.1	2.1	1.9
France	1.1	1.1	0.5	0.8	1.0	1.2	2.3	2.3	1.8	1.7	2.1	1.8
Italy	0.5	0.5	0.8	0.8	1.2	1.0	1.1	1.1	1.8	1.7	2.1	1.8
Spain	3.1	3.0	2.3	2.2	2.3	1.8	2.8	2.8	2.1	2.1	2.3	2.0
UK	0.9	0.9	1.4	1.5	1.5	1.5	2.5	2.5	2.8	2.4	2.6	2.1
Japan	-0.2	-0.2	1.1	1.2	1.0	0.9	2.6	2.6	2.1	2.1	1.7	1.8
China	4.7	4.8	4.5	4.5	4.3	4.2	0.3	0.4	0.8	1.0	1.4	1.5
World*	2.6	-	2.6	-	2.7	-	-	-	-	-	-	-

* Berenberg data at actual exchange rates, not according to purchasing power parities (PPP). PPPs lend more weight to fast-growing emerging markets
** Average, Bloomberg consensus as of 12/12/2024

LESS UPSIDE IN 2025, BUT HEALTHY MARKET BREADTH

IN A NUTSHELL

- US equities significantly outperformed all other equities in 2024. This clear divergence is unlikely to be repeated in 2025 for various reasons.
- 2025 is likely to be characterised by increasing M&A activity. European small caps in particular are likely to be targets due to the weak euro and favourable valuations. Market breadth should be correspondingly healthy in 2025, in line with a robust global economy. However, the upside potential for global equities is likely to be limited.

US equities clearly outperform in the fourth quarter

Our decision to add to US equities in the run-up to and immediately after the US elections paid off. With Donald Trump's election victory, the market also played out its "America First" policy. This was doubly profitable for euro investors invested in US equities. Not only did US equities rise sharply, but so did the US dollar. US small caps have gained more than 13% in euro terms so far in Q4. European and Asian equities, on the other hand, showed a volatile sideways trend in the same period. The difference in performance between US and European equities in 2024 is more than 23%, a record in this millennium.

Less regional performance divergence in 2025

With Donald Trump's victory in the US election, there is still a lot to be said in favour of US equities. After all, the new US president wants to advocate lower taxes, deregulation and an "America First" policy (including import tariffs) to strengthen the domestic economy. He also sees the stock market as a good barometer for his political successes, as we know from his first term in office. So there is a kind of Trump put similar to the Fed put. The president and the central bank have a vested interest in a robust S&P 500. After all, a rising stock market is accompanied by better corporate and consumer sentiment as well as higher tax revenues. Coupled with the great innovative strength of US companies in future technologies such as artificial intelligence, this clearly speaks in favour of US equities. However, we expect the divergence between US and European equities to narrow significantly in 2025, for several reasons. Although the majority of economists still expect the US economy to grow faster than the eurozone, they also expect the growth advantage to halve from around 2% in real GDP in 2024 to around 1% in 2025. Analysts take a similar view with regard to earnings estimates for 2025, with just under 15% expected for the US and just under 9% for the eurozone. By contrast, the expected earnings growth for 2024 is around 10% for the US and only around 1% for the eurozone. For European equities, there are many stumbling blocks and risks in addition to the threat of a trade war with China's weakness, the local economic slowdown, higher energy prices and the war in Ukraine. However, these are already reflected in share prices in the form of high risk premiums. Europe is currently trading at a record-high valuation discount of around 40% to US equities on a P/E basis. Given the record-high profit margins and the current P/E valuations of US equities, the starting position is more difficult than it was under Trump eight years ago.

US equities had never outperformed as strongly in this millennium as they did in 2024

Total return	YTD and in Q4 2024 (in %, in EUR): YTD (31/12/23-09/12/24)	Q4 24 (30/09/24-09/12/24)	12-month periods of the last 5 years (in %, in EUR): 09/12/23 09/12/24	09/12/22 09/12/23	09/12/21 09/12/22	09/12/20 09/12/21	09/12/19 09/12/20	P/B* 09/12/19	Div.* 09/12/19	P/E* 09/12/19
S&P 500	34.6	11.1	35.7	16.7	-8.3	37.8	9.3	5.1	1.3	22.5
MSCI USA Small Caps	24.6	13.4	30.1	5.7	-8.6	29.5	7.5	1.8	1.7	20.6
DAX	21.5	5.3	21.4	16.6	-8.1	17.2	1.8	1.7	2.7	13.8
MSCI EM Asia	20.8	0.2	23.1	-1.9	-14.5	6.3	21.2	1.7	2.3	12.9
Stoxx Europe Cyclicals	17.9	2.2	20.7	15.2	-8.9	25.2	0.8			
MSCI UK	16.9	2.4	18.8	4.7	8.0	22.9	-14.1	1.8	3.9	11.8
MSCI Japan	15.2	3.6	17.2	12.0	-11.2	13.1	2.2	1.4	2.3	15.2
Euro Stoxx 50	13.0	0.0	13.0	17.7	-3.9	21.6	-1.9	2.0	3.2	13.9
Stoxx Europe 50	11.2	-0.2	12.0	10.5	4.3	23.2	-4.3	2.4	3.4	14.3
Stoxx Europe Defensives	9.4	-2.4	9.8	7.0	5.0	18.4	-4.1			
Stoxx Europe Small 200	7.0	-1.5	11.1	5.4	-20.1	24.5	3.3	1.5	3.7	13.1
MSCI EM Latin America	-16.8	-4.1	-12.8	20.2	18.2	1.4	-19.2	1.5	6.2	8.5

Time period: 09/12/2019-09/12/2024.
Source: Bloomberg * P/B = price-to-book ratio; Div. = dividend yield (%); P/E = price-to-earnings ratio. Values based on estimates for the next 12 months.

Around USD1.1trn has flowed into US equity funds and ETFs since the beginning of this decade. The rest of the world has seen inflows of less than USD250bn in the same period. The extreme positioning and valuation are therefore susceptible to positive surprises from Europe and negative surprises from the US. An imminent end to the war in Ukraine and the Middle East could be a positive surprise. In addition, the favourable financial conditions (weak euro versus strong US dollar, widening interest rate differential between the US and Europe) should provide relative support for European companies.

Healthy market breadth in 2025 – also thanks to increased M&A activity

The weak euro and favourable valuations should make European companies attractive for private equity and foreign companies, particularly in the small cap sector. In the US, the imminent tax certainty for companies and a wave of deregulation are likely to boost not only the M&A market but also IPO activity. In addition to the robust economic environment, all of this should lead to a decent market breadth in 2025, in which second-line stocks are also likely to shine. For the S&P 500, we do not see any further valuation expansion in 2025, meaning that earnings are likely to be limited to earnings growth at most. For the rest of the world, it depends heavily on how many risks materialise. If many fail to materialise, European and emerging market equities should also receive support from valuation increases.

Ulrich Urbahn, Head of Multi Asset Strategy & Research

WHAT IS ON COMPANIES' MINDS?

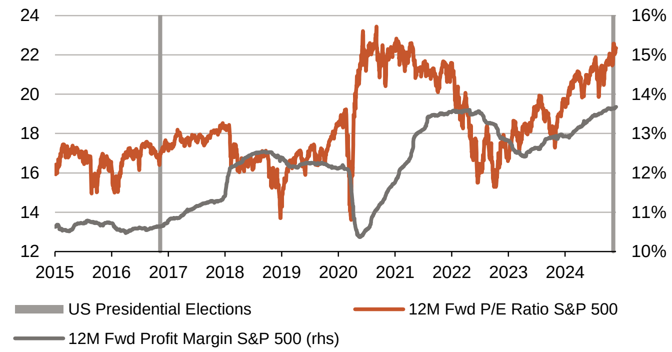
AI as a growth driver

AI, interest rates and the potential trade war dominated our discussions with companies in the past quarter. In the semiconductor industry, the wheat is being separated from the chaff. The broad sector is suffering from a sequential slowdown in China and only AI beneficiaries such as Marvell and TSMC are showing strength alongside Nvidia. Investors have therefore increasingly rotated into software companies in recent weeks – partly because they would be less affected by potential trade disputes and they expect further growth from AI applications in 2025. The expansion of data centres is also accelerating as a result of AI, and energy consumption is rising again for the first time after decades of stagnation in the US and Europe. On the other hand, fears of a trade war and the resulting potentially sharper fall in interest rates in Europe have put pressure on bank share prices, while stock exchange operators have benefited from the recent increase in market volatility. The prospect of further interest rate cuts has not yet contributed to an improvement in the order situation in the construction industry. On the consumer side, the negative trends have continued sequentially with a few exceptions, and the automotive industry in particular is currently struggling.

Matthias Born, CIO Equities

US equities with significantly higher expectations under Trump 2.0

P/E valuation based on earnings estimates for the next 12 months for US equities and the corresponding profit margin expectations



Time period: 01/01/2015–09/12/2024
Source: Bloomberg, own calculations.

Forecast summary: Moderate upside potential for 2025

Berenberg and consensus forecast in comparison, values for mid-2025 and year-end 2025

	Current			Ø*
Index forecasts	09/12/2024	30/06/2025	31/12/2025	In 12 months
S&P 500	6,053	6,200	6,500	6,601
DAX	20,346	21,000	22,000	22,293
Euro Stoxx 50	4,985	5,100	5,300	5,613
MSCI UK	2,382	2,450	2,600	2,728
Index potential (in %)				
S&P 500	-	2.4	7.4	9.1
DAX	-	3.2	8.1	11.7
Euro Stoxx 50	-	2.3	6.3	12.6
MSCI UK	-	2.9	9.2	14.0

* Average, consensus bottom-up as of 09/12/2024.
Source: Bloomberg, FactSet, Berenberg.

BONDS: TO WIN, YOU HAVE TO TAKE RISKS

IN A NUTSHELL

- Safe government bonds look attractive for hedging purposes, but offer little return potential.
- European corporate bonds offer at least fair, and in some cases attractive, yields.
- Emerging market local currency bonds offer the prospect of positive returns.

Bond markets between politics and economics

The final quarter of 2024 was dominated by politics: in addition to the ongoing Russian war against Ukraine and the conflicts in the Middle East, the US elections and the "red sweep", as well as the collapse of the German government coalition, complicated the situation. The consequences of these developments will not leave the bond markets untouched in the new year. What can we expect from the various segments of the fixed income asset class in 2025?

Safe government bonds with a cautious outlook

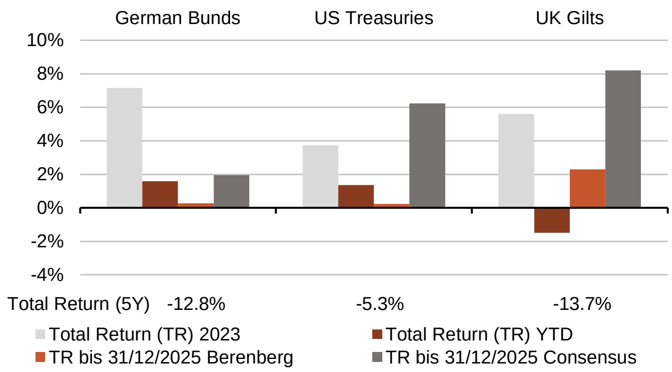
Unsurprisingly for us, the strong third quarter was followed by a weaker fourth quarter – yields rose on both sides of the Atlantic. All in all, 2024 was a mixed year for safe-haven government bonds and could be a foretaste of 2025, as we do not expect yields to provide significant support over the next 12 months. Although the fall in inflation will allow central banks to continue their rate cuts (bottom right), monetary easing will not be as strong as was expected a few months ago. In the US, optimism about rate cuts has been severely dampened as the change of government is likely to be accompanied by higher tariffs, stricter immigration policies, increasing price pressures and rising budget deficits. However, even in Europe, inflation will not return to pre-pandemic levels, which means that there is no room for yields to fall unless there is an economic slump or a further escalation of (geo)political conflicts. Against this backdrop, we consider safe government bonds to be of interest only as a hedge.

Corporate bonds: Perspective matters

Corporate bonds were the main beneficiaries of 2024 – the higher the credit risk, the better the performance. Better-than-expected economic performance in much of Europe and the US, as well as continued capital inflows, boosted demand. After the strong performance, however, risk premiums in the investment grade segment can still be described as fair at best and in the high-yield segment as increasingly unattractive. A look at yields, however, tells a different story and reveals fair and in some cases attractive valuations by historical standards. This is particularly true when compared to the negative and low interest rate environment from 2014 to mid-2022 (bottom left of next page). The combination of these two views, together with a more expansionary monetary policy and an expected stable economy, leads us to be cautiously positive on the corporate bond segment as a whole. However, further spread tightening is unlikely in 2025, meaning that the upside potential is likely to be capped by current yields. However, an increasingly likely market correction could brighten the somewhat gloomy picture and create opportunities for better valuation levels.

Safe government bonds offer only modest prospects

Past and expected performance of 10-year government bonds, overall effect of yield/price change, coupon yield and roll-down effect



Time period: 11/12/2019–11/12/2024
Source: Bloomberg, Berenberg calculations, iBoxx government bond indices (7-10 years, TR)

Forecasts: Key interest rates and government bond yields (in %)

Berenberg and consensus forecast in comparison, values at mid-year 2025 and at year-end

	12/12/2024	30/06/2025		31/12/2025	
	Current		∅*		∅*
USA					
Key interest rate	4.50-4.75	4.25-4.50	4.00	4.25-4.50	3.70
10Y US yield	4.30	4.70	4.15	4.90	4.10
Eurozone					
Key interest rate	3.15	2.40	2.35	2.40	2.20
10Y Bund yield	2.20	2.30	2.25	2.50	2.30
Great Britain					
Key interest rate	4.75	4.25	4.10	4.25	3.65
10Y Gilts yield	4.36	4.60	4.06	4.70	3.91

* Average, consensus as of 12/12/2024
Source: Bloomberg

Emerging markets: focus on the "phoenix from the ashes" countries

Donald Trump's election victory has recently been a clear driver of investor sentiment towards emerging market bonds, both local and hard currency. This is likely to continue in the first quarter of 2025. A restrictive tariff and immigration policy, as well as an unpredictable US foreign policy, are already a clear focus for emerging markets. So is there anywhere safe within the emerging markets asset class? The clear answer is yes, there are indeed emerging market issuers that have regained investor confidence thanks to fiscal reforms and the successful implementation of economic policy conditions imposed by the International Monetary Fund, as well as the strengthening of institutional independence from fiscal and monetary policy. These positive "recovery stories" have outperformed the broader emerging markets because of their idiosyncratic nature. This applies to both hard currency and local currency bonds. This trend should continue into the first quarter of 2025. Among the so-called "recovery stories" are Turkey, Egypt, Argentina, Serbia and India. An equal-weighted basket of these countries outperforms a broad local currency index in 2024 (bottom right). With high real yields, stable fundamentals, moderate currency risks versus the euro and low correlation to other asset classes, we see good opportunities for positive returns, particularly in the local currency segment.

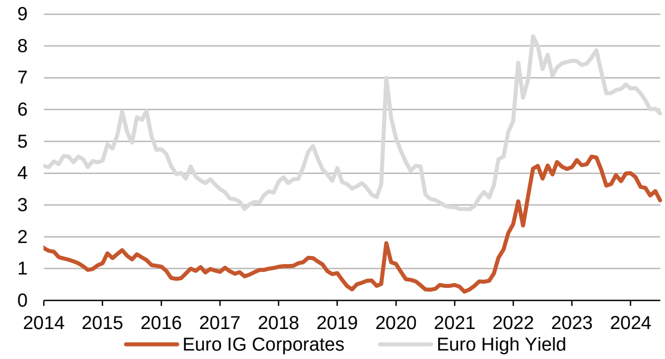
Conclusion: Our favourites are unchanged for 2025

After a weaker final quarter of 2024, safe-haven government bonds are unlikely to rally significantly in 2025. Only in the event of an economic downturn (not expected in our main scenario) or an escalation of geopolitical risks should they prove their worth as a hedging instrument, but otherwise they do not offer particularly attractive prospects. Euro corporate bonds should be viewed in a differentiated manner: They are expensive in terms of risk premiums, but still offer interesting opportunities in terms of yield levels. They are also supported by the ongoing interest rate cuts by the major central banks. In emerging markets, our focus is on recovering economies that have already demonstrated their potential last year and should continue to do so. Our main focus is on the local currency segment. The bottom line for 2025 is that if you want to make money from bonds, you have to take risks.

Martin Mayer, Senior Portfolio Manager Multi Asset
Felix Stern, Senior Portfolio Manager Fixed Income Euro
Wei Lon Sung, Senior Portfolio Manager Fixed Income Emerging Markets

Corporate bonds: yield levels remain attractive

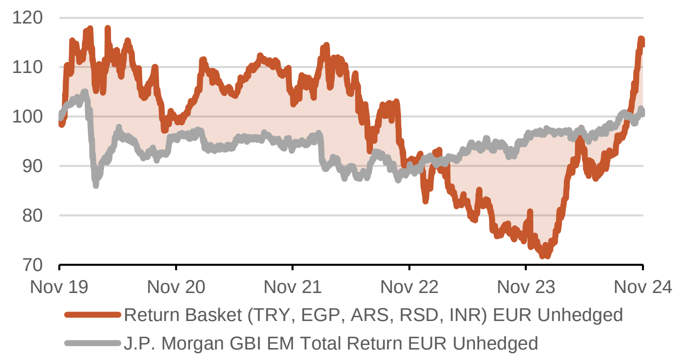
Euro-denominated corporate bond yields since the European Central Bank cut the deposit rate into negative territory for the first time in June 2014



Period: 31.12.2013-30.11.2024
IG = Investment Grade
Source: ICE, own presentation

Emerging market bonds: country selection continues to pay off

Performance of an equal-weighted basket of EM currencies (Turkish lira, Egyptian pound, Argentine peso, Serbian dinar, Indian rupee).



Period: 29.11.2019-29.11.2024
EM = emerging markets.
Source: Bloomberg, own calculations.

NOT ONLY GOLD SHINES IN THE LONG RUN

Oil continues to move sideways without geopolitical escalation

Crude oil remained stuck in a volatile sideways range in the fourth quarter of 2024. There was no new impetus from OPEC+, which had been keeping production levels artificially low for several months: in early December, the cartel once again postponed the planned production increases by three months to April. While Donald Trump's election victory had little impact, China's newly announced stimulus measures and geopolitical developments led to a volatile sideways movement in the oil price. Absent strong demand growth in China or a geopolitical escalation, a significant price increase remains unlikely given the abundant supply and weak demand outlook. However, a sharp fall in prices is also unlikely. The risks are well known and offer little potential for negative surprises. Trump's "drill, baby, drill" policy is also likely to be limited as oil companies focus on distributing profits rather than expanding production. As a result, the oil price is likely to remain volatile and overall sideways for the time being.

Gold has further upside after consolidation

Gold continued to rally in the fourth quarter, reaching new all-time highs. In early November there was a period of consolidation and gold fell by up to 8% at times. This was triggered by Donald Trump's election victory, which led to a sharp appreciation of the dollar, a temporary rise in bond yields and a risk-on mode in the markets. Previous strong performance, geopolitical easing and high positioning also made gold vulnerable to consolidation. Nevertheless, fundamental factors such as increased central bank and ETF buying, rising government debt, geopolitical risks and a downward trend in central bank interest rates should continue to support gold in 2025.

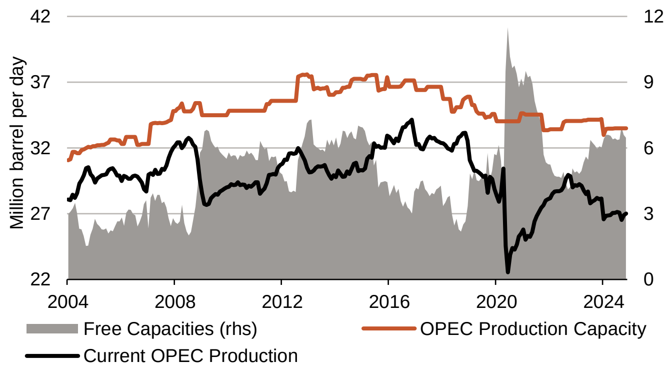
Structural drivers support industrial metals in the long term

Industrial metals were under pressure in the fourth quarter as manufacturing activity continued to weaken. Donald Trump's election victory also had an impact on the metals complex, as Trump's planned tariffs could weigh on Chinese exports and impact economic output, which in turn is likely to weaken demand for industrial metals. However, the downside potential is limited by factors such as a structural supply shortage, high demand as a result of decarbonisation and an economic recovery. In the short term, however, a significant recovery in the manufacturing sector will be needed for industrial metals prices to rise significantly.

Philina Kuhzarani, Multi Asset Strategy & Research

Crude oil price potential limited by high OPEC+ capacity

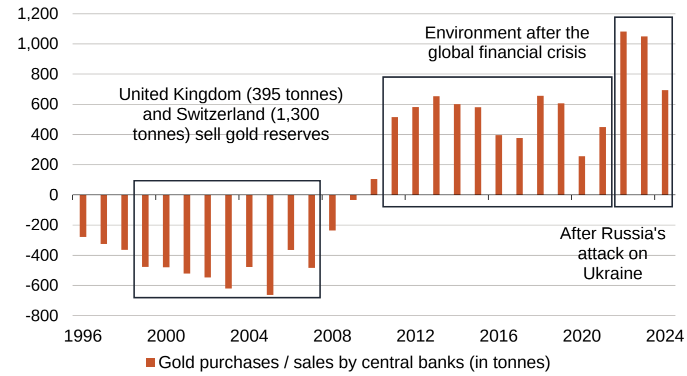
OPEC spare capacity over 20 years, in millions of barrels per day



Time period: 01/01/2004-30/11/2024
Source: Bloomberg, own calculations

Gold supported by central bank purchases

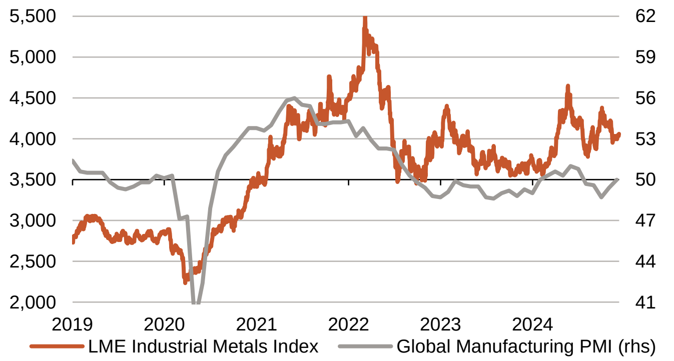
In 2022 and 2023, central bank purchases were already equivalent to around 25-30% of annual global gold production



Time period: 1995-31/10/2024
Source: World Gold Council, Bloomberg, own calculations, annual data

Economic upturn should strengthen prospects for metals

LME Industrial Metals Index versus the Global Manufacturing Purchasing Managers' Index



Time period: 01/01/2019-30/11/2024
Source: Bloomberg, own calculations

POLITICS REPLACES CENTRAL BANKS AS EXCHANGE RATE DRIVER

There is currently a lot in favour of the US dollar

A number of factors have recently provided a tailwind for the US dollar. A further escalation in the war of aggression against Ukraine and the ongoing conflict in the Middle East have boosted safe-haven demand for the greenback. In addition, US economic data has been surprisingly strong again in recent months, while eurozone data has been disappointing. In addition, the re-elected US President Donald Trump intends to further boost the already robust US economy through tax cuts and deregulation. Also, the import tariffs and stricter immigration policies he has announced will be inflationary. For the Fed, this creates a picture of stronger growth and higher inflation at the same time. This is likely to lead the Fed to cut interest rates by less than it otherwise would. In turn, higher interest rates mean that more capital will flow into the US, supporting the dollar. However, all of the above factors appear to have been priced into the euro-dollar exchange rate. If geopolitical tensions were to ease somewhat, if the US economy were to lose momentum or if the eurozone were to gain some momentum, the US dollar is likely to lose some of its strength.

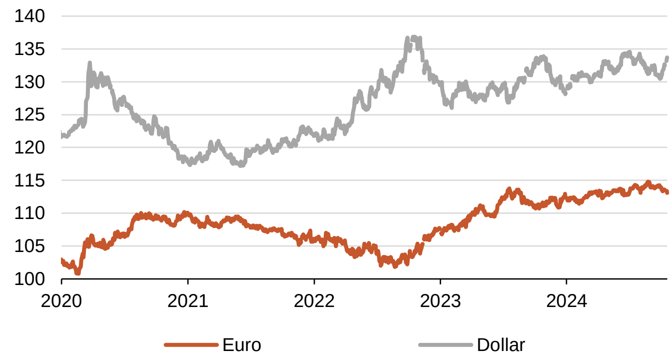
Trump's first concrete tariff threats against Mexico, Canada and China show that exchange rates react very quickly. Emerging markets in particular are at risk of seeing their currencies depreciate against the dollar in 2025 once an economy becomes the focus of Trump's tariffs.

Geopolitical uncertainties have also led to strong demand for the Swiss franc in recent months. However, the associated appreciation poses a challenge for the Swiss National Bank (SNB) as the strong franc makes imports cheaper, which, together with falling energy prices, threatens to push Switzerland into deflation. In October, the inflation rate fell again to 0.6% year-on-year, the lowest level since July 2021. The SNB attempted to counteract this in December by cutting interest rates by 50 basis points. However, as the key interest rate is now at 0.5%, the room for manoeuvre is limited. Direct exchange rate intervention by the central bank is therefore becoming more likely. We expect the SNB to try to stabilise the euro-franc exchange rate at around 0.95 in 2025.

Dr Felix Schmidt, Senior Economist

Trump gives the dollar wings

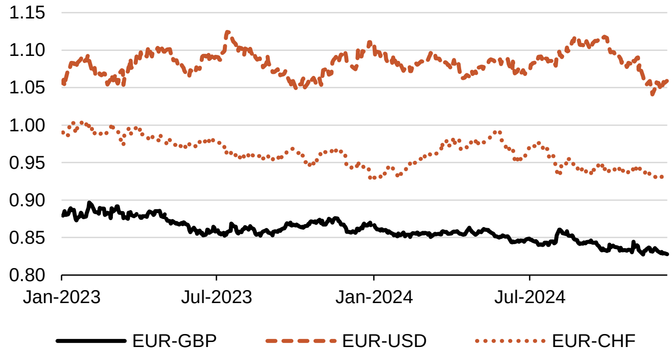
Nominal effective exchange rates



Time period: 01/01/2020-09/12/2024
Euro and dollar against trading partner currency baskets. Source: JPM

USD and CHF in demand as safe havens

Euro exchange rates



Time period: 01/01/2023-09/12/2024
Source: FT

Exchange rate forecasts

Berenberg and consensus forecast in comparison, values at mid-year 2025 and at year-end

	12/12/2024	30/06/2025		31/12/2025	
Exchange rate forecast	**Current**		**∅***		**∅***
EUR/USD	1.05	1.06	1.05	1.08	1.06
EUR/GBP	0.82	0.84	0.82	0.84	0.83
EUR/CHF	0.93	0.94	0.94	0.95	0.95
EUR/JPY	160	154	155	151	155
Change against the euro (in %)					
USD	-	-0.9	0.0	-2.8	-0.9
GBP	-	-2.4	0.0	-2.4	-1.2
CHF	-	-1.1	-1.1	-2.1	-2.1
JPY	-	3.9	3.2	6.0	3.2

* Average, consensus as of 12/12/2024
Source: Bloomberg

INTERVIEW WITH VINCENT KALMES

Mr Kalmes, you are a Luxembourger working for Berenberg in Frankfurt. How did that come about? And what do you particularly like about your job?

As a native Luxembourger, I started my career at a private bank in Luxembourg after working in France and England. During this instructive time as a securities trader, I realised that I wanted to focus more on the analysis of securities. Looking for a new international challenge, I came across a position at Berenberg that matched my professional goals and interests. So I joined the team in Frankfurt in 2020 and started working in Investment Consulting.

In my day-to-day work, I particularly appreciate the wide range of structuring options and the dialogue with experts across all asset classes. I am also fascinated by the complexities of the financial markets, which need to be deciphered for our clients.

You are head of the Multi Asset Internal Advisory team. What does that mean to you? What is your day like?

Our team is responsible for selecting securities for investment advice. We cover the entire process of recommending securities – from the initial idea to the detailed elaboration.

Our day's work begins with the daily market and product call for Berenberg's sales units. This provides us with valuable insights and impetus for the rest of the day. As the team is spread across the Frankfurt and Hamburg offices, we organise a daily team meeting to strengthen cooperation, coordinate tasks efficiently and react quickly to new market developments. Depending on the market situation, the focus may be on analysing and developing new ideas, monitoring current recommendations or commenting on quarterly results and price-driving news. We are also responsible for responding to specific client enquiries about the recommendations, as well as regulatory and technical enquiries.

Which clients are suitable for investment advice?

Investment advice is aimed at clients who want to play an active role in managing their portfolio and who want regular dialogue with their adviser. These clients should have a strong interest in learning about markets and investment ideas and in continually reviewing their investment strategy. Equally important is a willingness to make informed decisions within a reasonable timeframe in order to respond flexibly to changing market conditions.

Our client advisors incorporate the recommendations made by our team into an ongoing dialogue to identify new investment opportunities for our clients. This dialogue ensures that the recommended investments are best suited to our clients' specific circumstances and individual goals. The needs and concerns of our clients, as conveyed to us by their advisors, are crucial in shaping our investment advice.

What kind of asset classes do you cover?

Although our focus is on equities, it is important to have a balanced portfolio approach. We recommend that our clients maintain a diversified portfolio across asset classes. In addition to stock selection, fund solutions and certificates play a key role, as they are particularly suitable for thematic and tactical investments to take advantage of trends. Another important aspect is the careful analysis and selection of bond issuers to ensure stable returns. We recommend targeted commodity investments as an optimal complement to the portfolio. This holistic approach allows our clients not only to benefit from the opportunities offered by equity markets, but also to reduce volatility and achieve sustainable performance.

That sounds like a lot of topics. How do you manage that with your compact team?

We are a well-established team with regular dialogue and a structured approach. In addition, many of our tasks, such as reviewing changes in our advisory universe, are partially or fully automated. This allows us to focus more on the qualitative analysis of markets and investments, while at the same time meeting stringent regulatory requirements.

A key aspect of our work is the ongoing dialogue with many teams, in particular from our wealth and asset management, as this is the only way to cover such a wide range of asset classes and issues.

Which teams at Berenberg do you work with in particular?

We liaise regularly with the Multi Asset Strategy & Research team on asset allocation and tactical investment ideas. We also work closely with the Portfolio Management and Fund Selection teams.

At the same time, we work closely with the Professional Client Advisory team, which acts as a sparring partner for active investment advice to professional clients. Our team acts as a central interface between investment professionals and client advisors at our company. This means that our clients benefit not only from the expertise of the Berenberg Investment Platform, but also from a fast and effective exchange of knowledge. In particular, Berenberg's dynamism and short decision-making channels enable ideas to be developed quickly and turned into recommendations.

The market situation can change rapidly at any time. How do you deal with such volatility in your investment advice?

Our investment strategy is long term, with an average investment horizon of three to five years. This perspective forms the basis of our recommendations and enables us to bridge short-term market fluctuations and volatility. We also seek to diversify both sectorally and regionally in order to make our recommendations as stable as possible.

Despite this long-term focus, we recognise that there are always market events that can lead to unpredictable volatility – be they geopolitical crises, economic upheavals or other unforeseen developments. At such times, it is important to keep a cool head.

Together with the Multi Asset Strategy & Research team, we will prepare a communication to our clients if necessary, analyse the impact of the event on our existing recommendations and identify possible tactical opportunities.

SHORT VITA

Vincent Kalmes, CFA, joined Berenberg in 2020. At the end of 2023, he took over the management of the newly established Multi Asset Internal Advisory Team, which is responsible for the selection of securities in the investment advisory process. Previously, he gained valuable experience in Luxembourg at the private bank Banque de Luxembourg, where he worked in trading. Vincent holds a Bachelor's degree from the University of Aix-Marseille and a Master of Science in Investment & Finance from Queen Mary University of London and in Real Estate Investment from Cass Business School.

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IMPORTANT NOTICES

Date: 13 December 2024

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