Fiducian Monthly Economic Commentary Report

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Conrad Burge, Investment Manager, Fiducian Investment Management Services Limited

ECONOMIC OUTLOOK

GLOBAL ECONOMY

The global economy has continued to expand despite ongoing implementation of tight monetary policy by most major central banks. Since June, most major central banks have begun to lower their official interest rates as they seek to engineer 'soft landings' for their economies. In the IMF's view, inflation remains 'elevated in a few cases', while it sees a need for 'reforms that can revive productivity growth and attract capital'

The global economy has been able to sustain growth at close to its longer-term trend rate, despite tight monetary policy continuing to be implemented by most of the world's major central banks in an effort to lower inflation. Over the past year, inflation has been trending downwards, although in its latest report (January), the International Monetary Fund (IMF) noted that while global disinflation continues, it remains 'elevated in a few cases'. In particular, services price inflation remains a concern, with the IMF noting that it is 'still running above pre-Covid averages in many economies'. Nevertheless, official interest rates have been coming down, with the US central bank (the 'Fed') the European Central Bank and the Bank of England all lowering rates in recent months and with the IMF noting that 'monetary policy rates of major central banks are expected to continue to decline'. The IMF is also expecting tighter fiscal policy and would like to see 'targeted reforms in labour markets (and other sectors) that can revive productivity growth and attract capital'.

In the case of the US, recent data point to a rise in inflation once again, with this posing a challenge to both the 'Fed' and the new Trump administration. 'Fed' Chairman, Powell appears satisfied that monetary policy remains tight enough, while the President's pro-growth policies, including tax cuts, in the IMF's words, could 'spur near-term growth'.

In the case of the US, recent data indicates that inflation appears to be on the rise again, with the annual rate coming in at 3.0% in January (up from 2.4% in September). This comes after a drop in the official interest rate (the 'Fed funds rate') in recent months, with 'Fed' Chairman, Jerome Powell, stating on 12 February that 'the economy is strong, the labour market is solid and we have the luxury of being able to wait and let our restrictive policy work to get inflation coming down again'. The incoming administration under President Trump faces a host of challenges, including how to reduce excessive government spending. As Powell has previously noted, 'the US is on an unsustainable fiscal path'. The IMF adds that 'relaxation of unduly tight regulations may spur near-term US growth through higher investment', although 'uncertainties are high'.

AUSTRALIAN ECONOMY

The Australian economy entered a per capita recession in 2023 and remains weak, with households under cost-of-living pressure. Discretionary spending has fallen but some loosening of monetary policy has now begun.

The Australian economy remains weak, growing by only 0.3% in the September quarter. On a per capita basis, it remained in recession, contracting for the seventh quarter in a row (by 0.3%), with the economy unlikely to have gained much momentum since then. A key factor driving this slowdown has been tight interest rate policy by the Reserve Bank (RBA). This has weighed on household spending, with discretionary spending contracting over the year. In December, the RBA's preferred measure of annual inflation moved into the target range at 2.7%, leading to a small 0.25% cut in the RBA's 'cash rate' (to 4.1%) on 18 February.

MARKETS

Major share markets mostly rose over the course of 2024 but have been variable so far this year, with uncertainty weighing on the US market in particular. Most non-US markets still appear fairly priced.

Most share markets have been on a broadly upwards trend since October 2023 on the assumption that interest rates had peaked and would soon begin to be reduced. This has especially supported the more interest rate sensitive sectors of the market, including the technology and property sectors. This year, up to 27 February, the broad US market (S&P500), was flat, while the technology-focused Nasdaq fell 4%. Rising markets included the UK (7%), Germany (13%), China and Australia (each 1%), while Japan was down 4%.

Major sovereign bond markets saw yields rise after the end of 'quantitative easing' in 2022. However, since then slow growth in key economies has encouraged investors back into these 'safe havens' in many instances.

Major sovereign bond markets have been volatile this year, with yields (interest rates) rising and falling in line with the outlook for inflation. The US 10-year Treasury bond yield fell to a record low of 0.54% on 9 March 2020 during the pandemic but touched 5.0% in October last year before sliding down, then rising again. It was 4.26% on 27 February this year. Similarly, the Australian 10-year bond yield was 0.57% on 8 March 2020 but was 4.38% on 27 February 2025. Some bond markets could see yields fall (and prices rise) over coming months if growth remains soft and if inflation continues to fall back towards targets.

FIDUCIAN FUNDS

Fiducian's diversified funds are above benchmark for growth assets (shares and property), while cash is underweight.

Fiducian's diversified funds are currently above benchmark for international shares and listed property and around benchmark for domestic shares. Exposure to bond markets is close to benchmark, while cash holdings have been lowered.