Gibraltar Asset Management

STOCKBROKERS & INVESTMENT MANAGERS

Market Commentary - February 2025

FTSE 100	**8,700**	S&P 500	6,025
Resistance	8,800	Gold	$2,900
Support	8,270	GBP/EUR	1.2018
VIX	16%	GBP/USD	1.2409

Introduction:

The Nasdaq fell 3% in a single day late January on news DeepSeek, a Chinese startup, has released a large language model (LLM) more powerful and less expensive than established LLMs from Meta, OpenAI, and others. The AI market is growing, and we expect new entrants to continue to disrupt the market. However, whilst pricing is important, companies in the AI space prioritise relationships, continuity, speed, security, and reliability. Government policy is also highly likely to prevent wide adoption of Chinese LLMs, given risks of *"back doors"* to Chinese intelligence. In summary, the AI market is large and dynamic and will continue to face disruptions but the current incumbents are expected to continue to generate robust growth even amid increasing competition.

Market Outlook:

Over the long term *(since 1962), the FTSE All-Share has returned 7.2% per annum and that does not include the average 3.8% dividend yield earned on top. Therefore, 'strategically', it pays to be in the market. Also, considering inflation averaged 6.2% over the same period, it is vital that an investor invests in equities in order to preserve the purchasing power of their money. However, markets can be subject to swings in the interim and investors should be mindful of these with a view to protecting their capital and thus maintain a 'tactical' view.*

Our allocation to the stock market falls to equalweight. The stock market had two major events in the final two months of 2024. The first was the election of Donald Trump to a second term, which sent stocks soaring. The second was the more cautious tone from the Fed following the December FOMC meeting, which sent stocks falling. The Fed, so it seems, has yet to get the inflation genie *"back in the bottle"*. Yet consumers appear to be adapting to stubborn *"last-mile"* inflation and structurally higher prices.

In the background is a pending shift in market focus this year. For the past three years, investors have been attuned to monetary policy. The focus in 2025 likely will shift to fiscal policy, with America's new administration pledging further tax cuts. Other promised policies, including widespread tariffs and massive deportations, risk rekindling inflation.

Despite such policy uncertainty, the outlook for the economy and for corporate earnings is solid. Equity sectors are broadly rising and we continue to believe this breadth bodes well for 2025. Markets with good breadth tend to be more durable and better positioned to withstand adverse news than thin and narrowly led markets.

Last year, the market avoided any bone-rattling corrections. Selling spasms are positive in the long run but painful in the moment. But markets need to retreat in order to recover and make new highs. Given all the

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Market Outlook (cont):

risks outlined above, the stock market seems unlikely to go a second straight year without some level of stock turbulence. The FTSE 100 looks overbought at this time. A pullback would not be unexpected.

Market Commentary

Recommended Investment:

Investment Themes for 2025

In a certain-to-be-unpredictable investing environment, we present seven key themes (and seven low-cost ETFs to gain exposure) that we think will be important over the next 12 months.

1-Dividend Leaders

At this stage of the economic cycle, investors tend to pay close attention to companies raising dividends. We think consistent - and accelerated - dividend growth at a company gives three important signals to investors in a stock. First, the company's balance sheet is strong enough to pay a dividend. Second, management is mindful of shareholder returns, which include dividends. And finally, a significant dividend increase can be a message from management to the market that the near-term outlook for the company is promising, even during an economic slowdown. *SPDR S&P UK Dividend Aristocrats ETF trades on the LSE (UKDV.L) with a Total Expense Ratio (TER) of 0.30% per annum.*

2-Artificial Intelligence

The global AI industry annual revenue amounted to $250bn in 2024, and it is expected to grow at a 40% CAGR through 2030, when total revenue is forecast to reach $1.8tn. Although the industry is large and much development takes place within laboratories and universities, much of the revenue and most of the profitability from the AI industry is attributable to several US giants. *Roundhill Magnificent Seven ETF trades on the Nasdaq (MAGS) and provides equal-weighted exposure to the 'magnificent seven' (Alphabet, Amazon, Apple, Meta, Microsoft, Nvidia & Tesla) with a TER of 0.29%.*

3-Clean Energy

The rise in global land and sea temperatures, the melting of Arctic Sea ice, and the alarming frequency of extreme weather events (last autumn's hurricane season inflicted at least $200 billion in damages and 400 deaths) provide ample evidence that climate change is a reality. *iShares Global Clean Energy ETF trades on the LSE (INRG.L) with a TER of 0.65%.*

4- Sustainable Impact Investing

Sustainable Impact Investing, or ESG (Environmental, Social, and Governance) strategies, is gaining traction within the global investment community. According to the Global Sustainable Investment Association, global assets under management in ESG is on track for $50tn by the end of this year, up from $23 trillion in 2016. Instead of just identifying industries to avoid, the discipline now promotes *"sustainable"* business practices across all industries that can have an *"impact"* on global issues such as the climate, hunger, poverty, disease, shelter, and workers' rights. *iShares World SRI ETF trades on the LSE (SUWG.L) with a TER of 0.20%.*

5-Cybersecurity

The large number of well-publicised security breaches in recent years has forced businesses and government agencies to invest heavily in cybersecurity products and services to meet the challenge. Cybercrime is set to cost the world an estimated $10tn this year, compared to $3tn in 2015. These staggering cybercrime totals represent one of the largest transfers of wealth in the history of humankind. *L&G Cyber Security ETF trades on the LSE (ISPY.L) with a TER of 0.69%.*

6-Investing in the Cloud

Cloud computing has transformed the technology landscape over the past decade. Created almost accidently as a means of organising customer invoices, cloud has grown from the management of outsourced

Recommended Investment:

technology hardware resources to encompass tasks such as software development, big data analytics, and artificial intelligence. *First Trust Cloud Computing ETF trades on the LSE (FSKY.L) with a TER of 0.60%.*

7-Pharmaceuticals and Biotechnology
The use of prescription medication has risen some 60% over the last decade. What's more, the percentage of the population over the age of 65 has increased by 39%. This is important as it is estimated that a staggering nine out of 10 elderly adults take prescription medication and more than half of them report taking four or more prescribed drugs. While the elderly represents the majority of the prescription market, those under the age of 65 also are taking more medications than ever as treatments become available for chronic and rare diseases as well as weight loss and diabetes. *iShares Healthcare Innovation ETF trades on the LSE (DRDR.L) with a TER of 0.40%.*

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Post of the Month:

"Stagflation, an environment characterised by stagnant economic growth and persistent inflation, is the worst of all worlds. Companies are squeezed by slow growth and rising prices. Unemployment rises as the cost of living soars"

And rate-setters are finding themselves facing a horrible dilemma - should they fight inflation but slam the brakes on the economy? Or cut rates to stimulate growth and risk prices spiraling out of control?

Stubborn inflation and sluggish growth figures have given rise to stagflationary fears today. In the UK, unemployment has edged up to 4.4%, while price growth is expected to climb towards 3% later in the year. Even the buoyant US economy is not immune. Tariffs are expected to put upward pressure on inflation, while policy uncertainty under Trump could hobble growth.

Investors also fear stagflation - and with good reason. Stock markets sag under the dual forces of rising prices and slow growth, while bonds suffer as inflation erodes fixed incomes. History tells us that in times of stagflation, returns can be dismal. Analysts at Deutsche Bank call the stagflationary 1970s *"a terrible decade for equities and bonds across multiple countries"*. The data bears this out: US equities and Treasuries both saw real-terms declines, with long-dated bonds faring particularly badly. The analysts warn that in a stagflationary environment, *"it can be very difficult to generate positive real returns in most traditional financial asset classes"*. During the 1970s, only commodities, precious metals and property managed to eke out positive real returns.

But 'stagflation' has a very loose definition. Periods of economic stagnation and above-target inflation can be extreme (as we saw in the late 1970s), or far milder (as we see today). For now, the chances of a 1970s-style episode seem overblown - even allowing for policy surprises under Trump. Economists forecast that tariffs will be inflationary (perhaps taking US consumer price index inflation to 3%), but see no real chance of runaway price growth as a result. In a time of inflation targeting and independent central banks, inflation expectations are far better anchored. Although UK price growth is expected to rise, it will (probably) stay within the 1% threshold either side of the 2% target.

But 'stagflation-lite' still deserves our attention, not least for the fact that it makes it far more difficult to judge the path of interest rates this year. Markets expect limited easing from the Bank of England and the Fed in 2025. As it stands, investors probably need to prepare for a year of slow rate cuts, elevated inflation and sluggish growth.

History tells us that defensive stocks tend to fare better in these environments. Research from Schroders shows that since 1995, defensive sectors have outperformed during times of stagflation. Utilities, consumer staples, real estate and energy all outperformed when the stock market fell. IT, communications services, industrials, financials and materials all fared far worse - it is far easier to cut back on cyclical items as budgets come under pressure.

Analysts at Pictet Asset Management have named the unloved UK equity market their wildcard investment pick for 2025, citing the FTSE 100's potential as an attractive hedge against stagflation, thanks to its high proportion of energy and defensive sectors. Stuttering growth and rising prices can be horrible for economies - but could be rather good for UK large-cap stocks.

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Quote of the Month:

"Price is what you pay. Value is what you get" - Warren Buffett

Many investors focus too much on the price of an asset without considering its true worth. A stock may be cheap in price but still overvalued if the company has weak fundamentals. Conversely, a high-priced stock can be a great investment if it offers strong value through future growth and stability. Successful investing requires looking beyond short-term price fluctuations and assessing the long-term value of an asset.

Economics:

The Bank of England cut interest rates by another quarter percentage point at its recent meeting, bringing down the cost of borrowing to 4.5%. And in a sign that households can expect more cuts in the months to come, two members of the Bank's Monetary Policy Committee said they would have preferred to reduce rates even more, by a full half percentage point. However, the Bank slashed its forecast for economic growth, forecasting that the economy will skirt clear of a formal recession only by the narrowest margin in the coming months. The Monetary Policy Report and Bank forecasts signal that the economy is due to have another few years of weakness. They cut the forecast for economic growth this year, next year and the following year, as well as raising the inflation forecast. The Bank also warned that the tariffs threatened by Donald Trump on various economies posed a risk for economic growth in the coming years.

The eurozone economy stagnated in the fourth quarter as political instability weighed heavily on the region's two biggest countries, offsetting better performance elsewhere. That was the first time the economy had failed to grow since the fourth quarter of 2023, and a weaker outcome than the 0.1% growth expected by analysts. The annual growth rate stayed at 0.9%. European Central Bank President Christine Lagarde said risks to economic growth *"remain tilted to the downside,"* despite the Bank's latest policy easing, which cut the key deposit rate to 2.75%. The GDP is especially weighed down by France and Germany, whose economies actually contracted. The two together account for roughly half of eurozone GDP. France has lacked a stable government since elections in the middle of last year, while Germany faces early elections in February after its three-party governing coalition collapsed.

The US economy expanded at a solid pace at the end of 2024, fuelled by a generous tailwind from consumer spending that more than offset drags from a strike at Boeing and much leaner inventory investment. GDP increased an annualised 2.3% in the fourth quarter after rising 3.1% in the prior three-month period. Consumer spending, which comprises the largest share of economic activity, advanced at a 4.2% pace - the first time since late 2021 that outlays have exceeded 3% in consecutive quarters. The acceleration was the biggest since early 2023 and was led by a pickup in motor vehicle sales. The GDP figures cap another solid year for the world's largest economy that defied expectations for a marked slowdown as consumers hung tough in the face of persistent inflation and high borrowing costs. The economy grew 2.8% in 2024 after expanding 2.9% and 2.5% in the prior two years, respectively. That helps explain why the Federal Reserve is taking a more measured approach to future interest-rate cuts with Chairman Jerome Powell stating policymakers *"do not need to be in a hurry to adjust our policy stance"*.

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Seasonality: *"History doesn't repeat itself, but it does rhyme" - Mark Twain*

The January Barometer 🙂

Historically, the returns in January have signalled the returns for the rest of the year. If they are positive, the returns for the whole year tend to be positive and vice versa. First mentioned by Yale Hirsch in the Stock Trader's Almanac in 1972, a variant has it that returns for the whole year can be predicted by the direction of the market in just the first 5 days of the year. Judging by the first 5 days, 2025 is likely to be a positive year for the stock market.

February 🙂

Since 1984 the average month return of the FTSE 100 Index in February has been 0.6%, making it the 5th strongest month of the year. In an average February shares tend to rise strongly on the first trading day, then trade flat for a couple of weeks, before gaining strongly in the middle of the month and finally drifting off slightly to month end.

First Quarter 🙂

The FTSE 100 has risen 28 of the 41 years (68%) between 1984 and 2024, posting an average gain of 1.3%.

November - April 🙂

Delaying re-entering the market from St. Ledgers Day to Halloween has yielded statistically significant outperformance with the FTSE All-Share rising an average 13.4% from Halloween to May Day since 1965. There is a 1-in-2,000 chance of this arising by chance in random data. One explanation for this is that as the nights draw in during winter, we become anxious and depressed, which means share prices fall and expected returns rise. This then leads to a decent winter rise.

First-Year US Presidential Cycle ☹

The stock market tends to bottom out during the second year of each new presidential term and then recover strongly in the final two years. This is due to each Administration ensuring that the economy is strong by re-election time. Unfortunately, the excessive stoking of the economic fires creates excesses, including over-priced stocks, leading to poor stock market returns in the first two years of the next term.

Chinese New Year - Year of the Snake ☹

Chinese calendar revolves around a 12-year cycle where each year is associated with an animal (rat, ox, tiger, rabbit, dragon, snake, horse, goat, monkey, rooster, dog and pig). Each New Year starts between 21st January and 21st February, the exact date being dependent upon a variety of complex factors. The best performing animals since 1950 have been the goat and dog. The worst performing animals have been the rooster and snake. *In Chinese astrology, the Snake symbolises wisdom, caution, and strategic thinking. These traits might culturally inspire investors to adopt a more analytical or conservative approach. Interestingly, this is the Wood Snake Year, which comes about every 60 years. Wood represents expansion, innovation, and flexibility. This could favour industries like tech, renewable energy, and AI, which thrive on evolution.*

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Investment Calendar:

6th February	ECB Meeting
11th February	GDP Monthly Estimate (ONS)
12th February	Full Moon (markets tend to reach a low point around this time)
19th February	Consumer Prices Index Release (ONS)
21st February	Options Expiry Day
28th February	New Moon (markets tend to reach a high point around this time)

Technical Analysis:

Last month we were quite neutral on stocks from a technical perspective. All the indicators pointed to a flat market. In the event, the FTSE 100 rose 472 points or 5.7%. The market today looks far easier to take a view on. With the RSI at 66%, the market is approaching overbought levels. The market may be trending (the ADX is 31) but having broken through all resistance levels, it definitely appears overextended. Markets tend to revert to their 20-day moving average, which is 280 points below the current level. We are not saying a bear market is looming. But stocks need to retreat before setting themselves up for further advances. On that basis, we see a strong likelihood of a pullback in the coming weeks.

"The illusion of randomness gradually disappears as the skill in chart reading improves" – John Murphy

Chart Legend:

red dashed line	20 day moving average	(signifies the short-term direction of the security. prices tend to gyrate around their 20 day m/a)
thin red line	50 day moving average	(signifies the medium-term direction of the security)
thick red line	200 day moving average	(signifies the long-term direction of the security - whether it is in a bull or bear market)
blue line		(an indicator that measures 2 standard deviations away from the 20 day m/a)

Technical Analysis Guide:

RSI (relative strength index) - indicates whether a security is overbought (above 70) or oversold (below 30). Also when the RSI moves above 50 that is considered bullish (or vice versa).

ADX (average directional index) - indicates whether a security is in a trend (above 20) or not in a trend (below 20). For trending markets moving averages work best when considering lines of support/resistance. ending markets Bollinger Bands work best (sell at upper band, buy at lower band).

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