Market Update – February 2025

Asset class total return to 28/02/2025	1M (%)	3M (%)	6M (%)	1Y (%)	3Y (% p.a.)	5Y (% p.a.)	Current Yield (%)
Cash	0.3	1.1	2.2	4.3	3.5	2.2	4.1
Fixed Term Deposits	0.4	1.2	2.4	5.0	3.5	2.2	4.4
Australian Bonds	0.9	1.6	1.2	4.2	0.3	-0.6	4.3
Australian Bank Hybrids	0.6	1.0	2.9	6.5	3.6	3.5	5.1
Australian Property	-6.1	-7.6	-1.9	8.9	5.5	5.4	3.5
Australian Shares	-3.8	-2.6	2.8	9.9	9.2	8.9	3.4
Global Shares (unhedged)	-0.4	5.0	14.2	21.3	16.1	14.9	1.7
Global Infrastructure (hedged)	2.4	-1.8	3.4	18.0	4.8	4.8	3.6

Total returns and yields are before franking credits and fees. Source (in order): RBA cash rate, 12M Bank term deposit, Bloomberg Austbond Composite Index, Solactive Aust Banking Preferred shares Index, S&P/ASX 300 A-REIT Index TR, S&P/ASX 200 TR, MSCI World ex-Aust unhedged TR, FTSE Developed Core Infrastructure 50/50 hedged TR.

Financial indicator movement to 28/02/2025	1M	3M	6M	1Y	3Y	5Y	Price
AUD/USD (cents)	0.00	-0.03	-0.06	-0.03	-0.07	-0.13	0.62
Aust. 10-year bond yield (bps)	-0.13	-0.06	0.33	0.15	2.50	1.71	4.30
Gold US$/ounce (% p.a.)	2.1%	7.7%	14.2%	39.9%	30.2%	17.4%	2,859
Brent oil US$/bbl (% p.a.)	-4.7%	0.3%	-7.1%	-12.5%	1.3%	6.3%	73
Iron ore US$/t (% p.a.)	4.9%	4.5%	5.9%	-14.4%	4.8%	8.6%	107
Copper US$/pound (% p.a.)	6.0%	10.6%	8.9%	17.7%	15.8%	12.2%	4.51

Source: Refinitiv. Note: Past performance is not a reliable indicator of future performance.

Global wrap

The major focus in February was President Trump's policies addressing trade and government spending. It now seems that tariffs are more than a negotiating tactic and are likely to be applied to major trading partners (China, Canada, Mexico, Europe) on a more permanent basis. Similarly, Elon Musk and the Department of Government Efficiency (DOGE) have set about cutting the budget deficit in half from US$2 trillion.

While we understand that President Trump is addressing the US twin deficits – the US trade deficit and the US budget deficit – we see significant short-term disruption to US supply chains and the public sector. It is likely that US growth slows in the period ahead and indeed US bond yields have been moving lower. This means that the bond market is more worried about the growth outlook than any inflation threat from tariffs.

There are clear risks here for the US share market, which has rallied 66% from its October lows and trades on a forward P/E around 22x (on forecast earnings growth of 12%). If US growth slows, then obviously earnings growth could be at risk, along with market valuations.

On a more positive note, the global easing cycle continues in Europe, while China is expected to offer more internal stimulus to offset the potential negative impact of US trade tariffs. Indeed, Chinese share markets remain buoyant, and commodity prices have generally been strengthening (oil and lithium being the major exceptions).

Australian wrap

The big news in February was the RBA cutting the cash rate by 0.25% to 4.10%. Headline inflation (2.4%) is already within the RBA's 2-3% target range, while core inflation (3.2%) should move within the target range by the March 2025 quarter. The RBA is hawkish on any more rate cuts, but the market doesn't believe it and is pricing in 50bps (0.50%) of rate cuts by September 2025.

That said, the easing cycle is likely to be relatively shallow this time around as the cash rate is only a little above neutral (3.5%), while employment has been more resilient than expected (mainly due to government spending). In addition, the Australian economy has been gaining momentum, with December quarter GDP growth of 0.6% (2.4% annualised), although annual growth is still low at 1.3%.

The recent 1H25 company reporting season showed very mixed results, with low earnings growth (on aggregate) and dividends generally being reduced. This is mainly attributable to weakness in the Resource and Energy sectors. However, the outlook for earnings should improve in FY26 based on an RBA easing cycle and a good chance that China stimulus will see a recovery in commodities.

The Federal Government is preparing for an election that is due before 17 May 2025. Government spending remains high and with commodity prices easing over the past year, it is likely the Federal Budget will be moving back into deficit in FY25.

The housing market has been flattening off in major cities as affordability and taxes become a major issue. This easing cycle may see limited upside in house prices until affordability becomes more evident.

Outlook

The outlook is decidedly mixed with the positives of a global easing cycle clouded by aggressive changes to US trade and fiscal policy. There is a rising risk of short-term disruption to the world's largest economy and its listed companies. And with the US share market elevated after a strong 2-year run, there is an increased chance of a market correction.

We have elected to move from a bullish position back to a cautious position. We are not outright bearish because easing interest rates are a major positive and most markets, outside of the US, seem reasonable value.

Rather, we think it is prudent to take a cautious short-term view to observe the fallout from Trump's policies and its impact on the US economy and financial markets. In short, we do expect a US market correction, but we are not expecting a bear market, as yet. Further, we expect markets to become more volatile during 2025 and for investment skill to become more important over simple index hugging strategies.

Key known risks

1. Trump's policies upset global trade and the US economy;
2. Inflation starts to rise again;
3. China's economy disappoints on growth; and
4. Geopolitics and/or climate change events impact economic activity.

Next key events

- Fed meeting – 19 March 2025
- RBA meeting – 1 April 2025
- Australian Federal election – due before 17 May 2025

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Warnings, Disclosures and Disclaimer

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