Discovery Global Multi-Asset Fund

31 December 2024

Market background

Markets experienced a mixed fourth quarter, shaped by significant geopolitical and macroeconomic developments. The US presidential election, the key market event, initially boosted sentiment toward US assets but also introduced policy uncertainty. Inflation concerns rose as macroeconomic data and Trump's proposed import tariffs signalled potential pressures.

Central banks remained cautious. The US Federal Reserve (Fed) delivered a final 25bps rate cut in December, prompting markets to recalibrate expectations for future easing. The European Central Bank (ECB) continued its 25bps cuts and downgraded its growth outlook, while the Bank of Japan (BoJ) held its policy rate at 0.25%. The People's Bank of China (PBoC) signalled a shift toward a 'moderately loose' monetary policy for 2025.

Global equities delivered flat returns overall, with significant divergence. Developed market equities outperformed emerging markets, with market leadership narrowly concentrated. US equities posted low-single-digit returns, bolstered by strong performance after the election. Mega-cap tech stocks held their ground, while small caps lost momentum. European and Asian equities struggled under tariff risks, weak economic data, and diminished global risk appetite, while Japanese equities outperformed, aided by a weaker yen.

Risk assets delivered mixed results. Global high-yield corporate bonds posted small negative returns. The US dollar strengthened as investors weighed tariffs and recalibrated rate expectations, pressuring emerging market debt, particularly local currency bonds. Commodities were mixed.

Defensive assets remained under pressure, with developed market sovereign bonds losing ground. Inflation fears weighed on US Treasuries, and rising yields linked to tariffs overshadowed Europe's weaker growth outlook. UK gilts also declined, while higher rates negatively impacted investment-grade corporate bonds. The yen weakened against the US dollar as the Fed's stance contrasted with the BoJ's dovishness.
Gold prices declined during the quarter.

Performance review

The Fund delivered a negative absolute return in US dollars, gross and net of fees, but outperformed its benchmark (60% MSCI AC World NR40% Citigroup WGB).

The net overweight position to equities provided some offset as risk assets succeeded in shaking off the global risk-off tone and uncertainty in the lead-up to the US election. Broad index exposure to the US through Nasdaq and Russell futures benefitted from the significant post-election rally in regional equities. Security selection was a small detractor on a relative basis. Sector-specific challenges in healthcare and semiconductor positions in the US and Europe detracted amid disappointing earnings and growing uncertainty over the potential impacts of Trump's anticipated policies, including upside risks to inflation and discount rates.

In fixed income, an overweight to developed market duration detracted from relative returns in the latter part of the quarter. Bond markets faced headwinds from rising yields as investors adjusted expectations for interest rate cuts amid persistent inflation concerns and heightened uncertainty around fiscal and tariff policies, particularly in the US. A hawkish shift by the Fed in the final weeks of the quarter further intensified these pressures.

Currency positioning was a contributor to relative performance, with long US dollar positions benefitting from supportive macroeconomic dynamics, in particular the US economy's relative outperformance and heightened uncertainty of the US election. Gold also contributed positively to relative returns.

In Q4, global markets navigated a challenging environment marked by heightened policy uncertainty following the US election, stronger-than-expected inflation data, and shifting central bank expectations adding to volatility. Against this backdrop, the Fund adjusted its positioning to reflect a more balanced risk-reward outlook.

Overall, the net equity overweight ended the quarter at c.13% overweight relative to the benchmark exposure, c. 1% higher than at the start of the quarter. The portfolio added Nasdaq futures, following a reset in positioning and expectations of a supportive environment, driven by stable US growth and anticipated policy easing, which was largely offset by profit-taking in US small cap futures, as well as in individual outperforming companies such as Visa, Mastercard and Aecom after a sharp rally in US risk assets post-election. Profits were also taken in specific Chinese companies post strong performance supported by China's economic stimulus. This was largely offset by an initiation of Hang Seng futures towards the end of the period, given a desire to keep exposure stable reflecting optimism around China's shift to a "moderately loose" policy stance for 2025. Exposure to semiconductor index futures (SOX) was rotated into S&P 500 futures due to weaker relative momentum and rising tariff risks associated with a potential Trump presidency.

In fixed income, overall duration fell over the quarter by 1.3 years, taking the portfolio underweight 0.9 years relative to the benchmark driven by a reduction in US government bond exposure. This reduction was offset by an addition to UK government bonds, and small additions to Germany and Australia.

The portfolio maintained its US dollar overweight over the quarter. A position in gold was also closed over the quarter, locking in gains as prices reached extended levels with the high level of uncertainty ahead of the US election.

Outlook and strategy

In the US, monetary policy has been eased to support growth and protect the labour market. However, Trump's election victory has introduced uncertainty regarding inflation. In response, the Fed appears to be more cautious about further easing. Policies of deregulation and tax cuts are expected to bolster growth, while tariffs and proposed immigration measures may exert upward pressure on inflation.

Our central outlook for the US economy in 2025 anticipates relatively robust growth, with inflation consolidating toward target despite some volatility. Higher bond yields and uncertainties around trade policies could contribute to near-term volatility in US risk assets.

In Europe, monetary policy has also been eased, but conditions remain relatively tight. Growth indicators have been weak, with some countries nearing recession, while short-term inflation measures align with the ECB target. We expect eurozone growth to remain subdued and inflation to moderate further. The ECB's easing cycle is likely to be more pronounced than the Fed's, given structural challenges in the eurozone and risks posed by potential US tariffs.

In China, easing measures are becoming increasingly aggressive, with policymakers prioritising domestic demand expansion. Additional announcements are expected following recent key policy meetings. Authorities appear determined to ensure a sustained recovery, though growth remains uneven and inflation weak. However, base effects should provide some inflationary support going forward. We believe the Chinese economy will fare better than bearish consensus views suggest, given the escalating policy response.

Reflecting our central investment roadmap, we reduced exposure to US equities in December and early January, recognising elevated sentiment and heightened uncertainty surrounding tariffs in the first half of the year. This positioning enables us to take advantage of potential market weaknesses. In fixed income, we maintain a significant allocation to defensive government bonds to hedge downside risks and prepare for opportunities during market volatility. In currency, active positions remain limited, with the US dollar at a pivotal juncture. Its trajectory will likely hinge on the Trump administration's trade policies in the months ahead.