

Hymans Robertson Investment Services (HRIS)

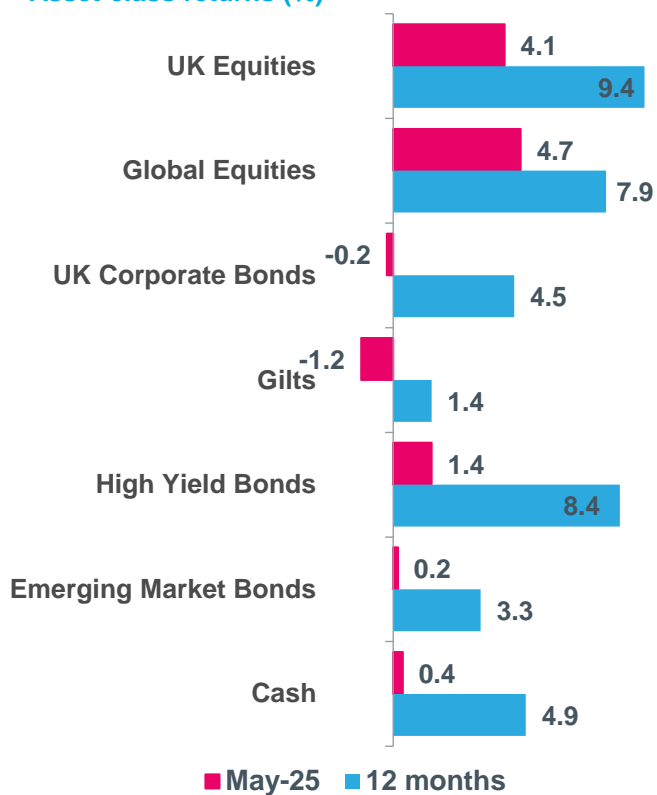
Market digest

May 2025

Monthly highlights

- Markets rebounded in May from the initial shock of Trump's tariff announcements.
- US equity markets, in particular, performed well but bonds were more mixed following fiscal concerns in the US Treasury bond market.
- On page 3 of this document, we provide market commentary to cover the 12 months to 31 March 2025.

Asset class returns (%)



Source: Morningstar. Figures to 31 May 2025. Returns in sterling terms except high yield bonds which are hedged. EM bonds are 50% local currency denominated and 50% US dollar denominated bonds.

Market summary

- Our model portfolios typically invest in a combination of the asset classes shown in the left-hand chart.
- Equity markets recovered losses sustained in April as investors' concerns over tariffs eased. Progress with negotiations between the US and its trade partners led to optimism that the eventual tariff rates will be much lower than those announced on "Liberation Day".
- The US market was the best performing equity region, rebounding from a poor April. The global equity market recovery was broad based though, with the UK also notching up strong returns of 4.1%. However, the various twists and turns of the trade negotiations ensured volatility remained high.
- Performance was not as good in bond markets. Concerns over higher US government borrowing were exacerbated by the passage of Trump's "Big, Beautiful Bill" through Congress. This was highlighted by Moody's downgrade of the US' credit rating from AAA to Aa1.
- Bond yields, including UK government gilts, rose as a result (bond prices fall as yields rise).
- At a portfolio level, equities tended to outperform bonds, resulting in higher risk portfolios producing greater returns than lower risk portfolios over the month.

Outlook and topical market themes

- A court ruling challenging Trump's tariffs has added legal uncertainty to trade policy, but markets appear less reactive (and potentially complacent), reflecting investor fatigue and growing scepticism about the durability of tariff threats.
- Rising yields on long-dated US and global government bonds, driven by concerns around fiscal sustainability, are creating potential opportunities for long-term investors, despite ongoing volatility.

Court ruling adds to tariff uncertainty

On 28 May, the US Court of International Trade ruled that Trump's blanket tariffs were illegal, stating that the President does not have the power to justify them under emergency economic powers. However, the very next day, an appeals court allowed the tariffs to remain in place – for now. The court wranglings add another dimension to the ongoing tariff negotiations and further deepen the uncertainty facing consumers and businesses. Although equity market volatility remains elevated, there are signs that investors are growing weary of the see-saw nature of tariffs. Market reaction to tariff announcements have become more muted. For example, when Trump announced 50% tariffs on the EU on 23 May, the US equity market fell just 0.7% (by the weekend, the tariff rate had been cut once again). Compare this to the 3 April (the day after Liberation Day) when the US market fell almost 5%. Wall Street, never short on acronyms, has adopted a new one: TACO – Trump Always Chickens Out. Increasingly, it seems the market is beginning to believe it.

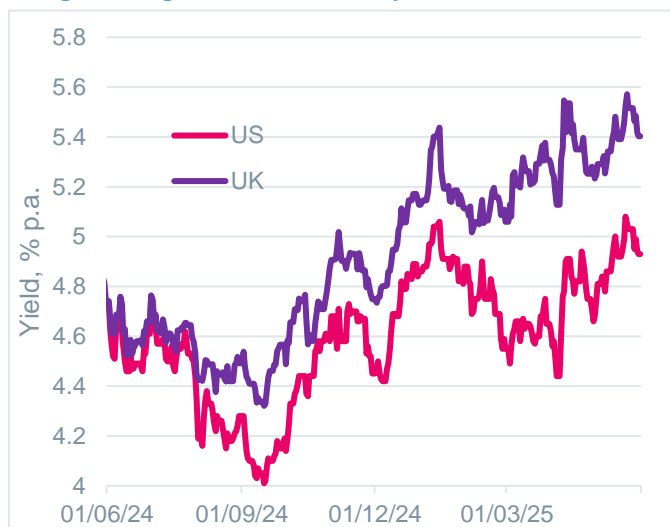
Short-term pain, long-term gain? What the bond volatility means for investors

Although most investors were focused on the equity market in April, it was the bond market that drew attention in May, as yields on long-dated government bonds climbed (prices fell as yields rose). Much of the pressure stemmed from growing concerns about fiscal sustainability. President Trump's "Big Beautiful Bill" is expected to add trillions of dollars to the US government debt, raising expectations for increased bond issuance and increasing yields as a result. Moody's, the credit rating agency, added to the pressure by downgrading the US government's credit rating to Aa1, following similar moves by S&P in 2011 and Fitch in 2023.

The yield on 20-year US Treasury bonds rose from 4.7% at the end of April to a peak of 5.1% on 22 May, before easing slightly towards the end of the month. Bond market volatility wasn't confined to the US. Investors also put pressure on gilts and Japanese bonds where government debt sustainability is also a concern. In fact, many investors believe it's the Japanese bond market driving US yields, not the other way around. If Japanese yields increase, they become more attractive to Japanese investors who then switch from other holdings such as US bonds, therefore driving US yields up. It's worth noting, while fiscal concerns are real and deserve attention, the recent rise in yields may present an opportunity for long-term investors willing to take on the associated risks.

Chart of the month

Long dated government bond yields have continued to rise



The chart shows the yields on 20-year government bonds for the US and the UK over the past year.

Yields spiked following President Trump's Liberation Day tariff announcements, before easing slightly. However, over the past month, they have resumed their upward trend as investors demand higher returns to compensate for growing concerns about fiscal sustainability.

Source: Bank of England 20-year gilt, St Louis Fed 20-year US Treasury



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Annual market summary: covering the 12 months to 31 March 2025

The key question for investors through 2024 was how fast central banks would start to reduce interest rates. As it turns out, the re-election of Donald Trump was of more importance over the period. A close election was expected, but what we got was an emphatic victory for Trump. Markets quickly pivoted towards 'Trump trades' reflecting the expected winners and losers from Trump's expected policy agenda.

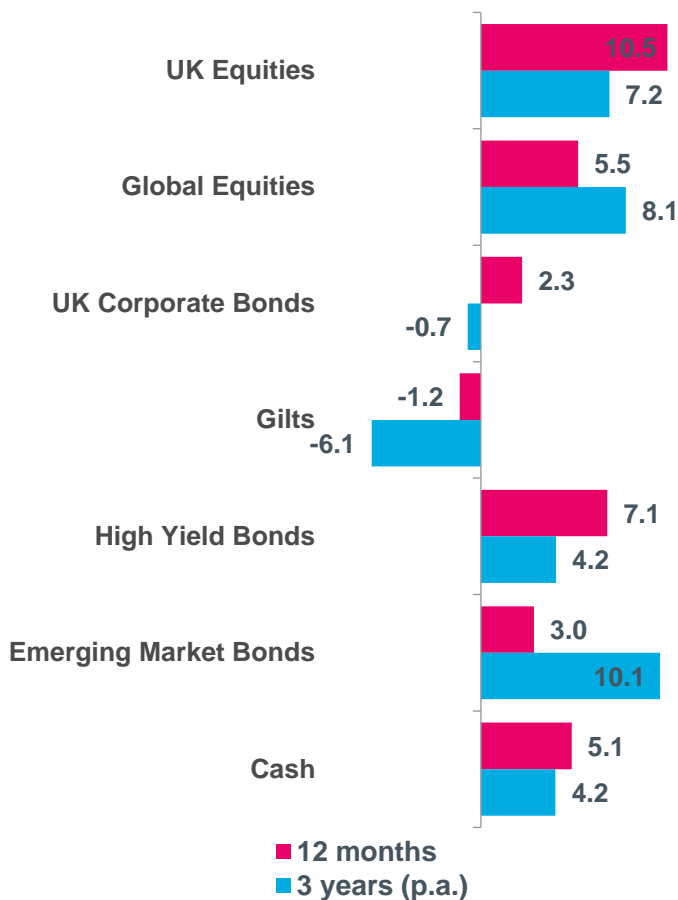
However, investors' early enthusiasm for President Trump's policy agenda started to wane, and then completely evaporated, as Trump prioritised implementing heavy tariffs on trade partners, as opposed to working on the more market friendly policies such as tax cuts and deregulation.

Central banks started on their path towards lower interest rates. The Bank of England cut by 0.75% over the period to 4.5%, while the US Federal Reserve cut rates by 1%. Trump's tariff policies have led to greater uncertainty over the near-term path for interest rates in the US, as inflation is expected to rise in the short term at the same time as economic growth slows.

The first three quarters of the period were largely positive for equity performance, but some gains were given back in Q1 2025. The UK equity market ended the period as one of the top performing regions, after the US market fell heavily in Q1 25.

Bond performance was mixed over the period, as expectations on inflation and interest rates were ever changing. Although central banks began their rate cutting cycle, bond yields ended up rising over the period. Trump's election victory was a big driver of bond yields upwards, as was the Budget in the UK, and German fiscal stimulus announcements. On top of that, strong US economic growth, and sticky inflation, lowered expectations as to how far central banks will cut rates. Given these events, gilts fell over the period. Performance on corporate bonds, especially high-yield bonds, was better as credit spreads (the additional yield on corporate bonds over government bonds) fell, pushing up prices.

Asset class returns (%)



Source: Morningstar. Figures to 31 March 2025. Returns in sterling terms except High Yield Bonds which are hedged. EM bonds are 50% local currency denominated and 50% US dollar denominated bonds.

Risk warning

The value of your investments and the income from them may go down as well as up and neither is guaranteed. Investors could get back less than they invested. Past performance is not a reliable indicator of future results. Changes in exchange rates may have an adverse effect on the value of an investment. Changes in interest rates may also impact the value of fixed income investments. The value of your investment may be impacted if the issuers of underlying fixed income holdings default, or market perceptions of their credit risk change. There are additional risks associated with investments in emerging or developing markets. The information in this document does not constitute advice, nor a recommendation, and investment decisions should not be made on the basis of it. The material provided should not be released or otherwise disclosed to any third party without prior consent from HRIS.