CAIM | CROWN AGENTS INVESTMENT MANAGEMENT

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CAPITAL MARKETS MONTHLY

FIXED INCOME

CHARLES THOMSON

HEAD OF PORTFOLIO MANAGEMENT

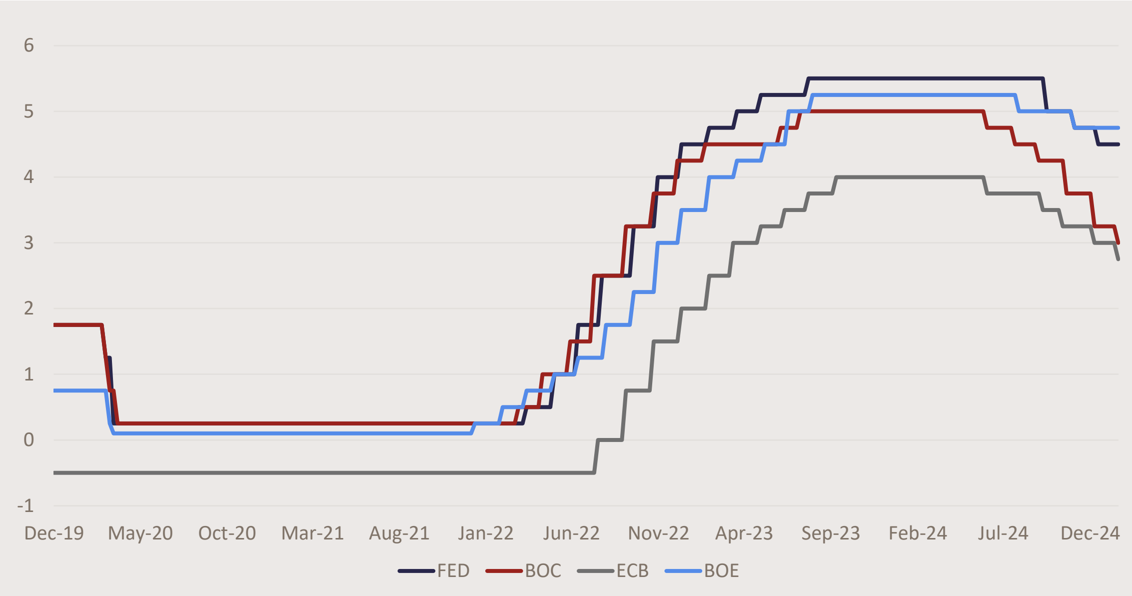
Yield Volatility Remains Elevated as Macroeconomic and Geopolitical Uncertainties Persist

As expected, the Federal Reserve maintained unchanged interest rates at the January FOMC meeting. The upper band of the Funds rate therefore remained at 4.5 percent. The FOMC statement was amended to a slightly more hawkish commentary regarding inflation, which remains above the Federal Reserve's target level. Labour market strength was also highlighted following the solid Non-farm Payroll growth, announced on 10th January by the Bureau of Labour Statistics, with a decline in the unemployment rate from 4.2% to 4.1%. However, the monthly inflation report on January 15th showed an unexpected decline in core inflation, from 3.3% to 3.2% which resulted in a reversal of the direction of US Treasury yields. Having traded as high as 4.42% immediately following the employment report, the benchmark US Treasury 2-year note yield steadily declined in the second half of January to close the month at 4.20%, which is around four basis points lower than the start of the year.

There is significant downward pressure on short term interest rates globally. Both the Bank of Canada and the European Central Bank cut rates in January. The BoC has now reduced the overnight lending rate from 5.00% to 3.00% over the past six months while the ECB has lowered the deposit rate from 4.00% to 2.75% over the same period. A further 0.25% cut from the Bank of England is expected on 6th February, which will take the bank rate to 4.50%. A deteriorating economic outlook with below-trend GDP growth is the main driver of further monetary policy easing.

The chart below showing the path of G7 short term interest rates (excluding Japan).

Monetary policy easing continues in Europe and North America



Source: Bloomberg Finance L.P., January 2025.

During January 2025 there were thirty-five Sovereign, Supranational and Agency borrowers in USD with amount outstanding of at least USD 300m, credit rating at least A- and maturity between 1 and 10 years. As anticipated, there was a significant amount of issuance in the SSA sector in January 2025. We participated in several transactions including OPEC, CABEI, IFC, CCMM, CAF, British Colombia and EIB. These transactions all performed well as spreads versus government benchmarks narrowed.

Issuer	Maturity	Issue Spread	Rating
Asian Development Bank	14/01/2028	10	AAA
Development Bank of Japan	16/01/2035	27	A+
European Investment Bank	14/03/2030	28	AAA
Export-Import Bank of Korea	14/01/2028	30	AA
Export-Import Bank of Korea	14/01/2035	63	AA
International Bank for Reconstruction & Development	15/01/2032	37	AAA
Clifford Capital Pte Ltd	14/01/2030	38	AAA
Council Of Europe Development Bank	15/01/2030	39	AAA
Export-Import Bank of Korea	14/01/2030	40	AA
Inter-American Development Bank	15/02/2030	41	AAA
Kommunalbanken AS	15/01/2030	42	AAA
Province of Ontario Canada	15/01/2030	43	AA-
Agence Francaise de Developpement	16/01/2030	44	AA-
Airport Authority	15/07/2028	45	AA+
Asian Infrastructure Investment Bank	16/01/2030	46	AAA
Landeskreditbank Baden-Wuerttemberg	14/01/2028	47	AA+
BNG Bank NV	01/02/2030	48	AAA
Caisse d'Amortissement de la Dette Sociale	22/01/2030	49	AA-
Corp Andina de Fomento	22/01/2030	50	AA
International Finance Corp	21/01/2028	51	AAA
Kreditanstalt fuer Wiederaufbau	18/03/2030	52	AAA
Province of British Columbia Canada	24/01/2028	53	AA-
Kuntarahoitus Oyj	02/02/2029	54	AA+
CDP Financial Inc	24/01/2030	55	AAA
Central American Bank for Economic Integration	24/01/2028	56	AA
Dexia SA	24/01/2030	57	AA-
Kommuninvest I Sverige AB	09/02/2028	58	AAA
NRW Bank	24/01/2028	59	AA
Oesterreichische Kontrollbank AG	24/01/2030	60	AA+
Province of Saskatchewan Canada	28/01/2030	61	AA
NEDFIN	26/04/2028	62	AAA
OPEC Fund for International Development	03/02/2028	63	AA+
Caisse des Depots et Consignations	31/01/2028	64	AA-
Korea Development Bank	03/02/2030	65	AA
Korea Development Bank	03/02/2028	66	AA

Source: Bloomberg Finance L.P., January 2025.

FOREIGN EXCHANGE

SLAWOMIR SOROCZYNSKI

HEAD OF FIXED INCOME

FX Market Adopts a 'Wait and See' Approach as Trade Wars Loom

The foreign exchange (FX) market entered 2025 on a cautious note, with investors carefully analysing the final trading weeks of the previous year. During this period, the US dollar surprised many by extending its upward trend from prior months. However, in January the upward momentum dissipated, and the greenback was moving with lack of clear direction. This 'limbo' was further exacerbated by central bank meetings and the long-anticipated change of leadership on Capitol Hill.

As a result, most currency pairs remained within a narrow ±1% deviation range. The Japanese Yen outperformed its peers, appreciating by 1.4% and ending the month as the best-performing G10 currency. Meanwhile, high-beta currencies showed mixed results: the New Zealand dollar advanced 0.70% against the greenback, while the Canadian dollar lost 1%.

This high uncertainty in the market was probably best reflected in gold prices, which had one of their strongest trading months on record. Gold surged nearly 7% to a new all-time high. (For a detailed breakdown of G10, SDR, and gold performance, please refer to the accompanying table.)

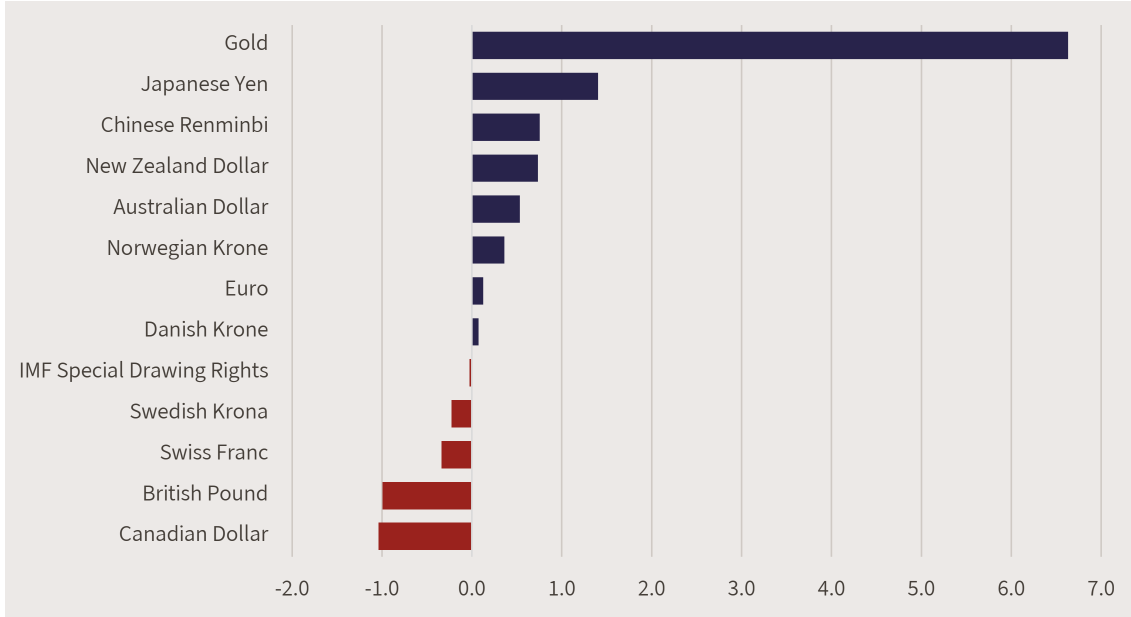
Looking ahead, market participants will closely monitor policy decisions and statements from President Trump, with particular focus on actions targeting China. Investors are positioned bearishly, expecting further renminbi weakness. As China prepares to celebrate the Lunar New Year in early February, those exposed to onshore versus offshore renminbi (CNH) markets should brace for heightened volatility. The onshore market will be closed, while offshore trading in CNH will continue.

Beyond US-China trade tensions, European politics is set to be another source of uncertainty in February, with Germany's federal elections scheduled for February 23rd. Additionally, economic divergence among G10 nations is expected to attract the attention of investors and central banks. We anticipate most central banks will continue adjusting their monetary policies. However, geopolitics remains the dominant factor influencing financial asset valuations worldwide.

With this backdrop, we expect previous trading ranges to be tested, with short-term risks tilted toward further US dollar strength. For EUR/USD, we anticipate a test of 1.0320, followed by 1.0200, though we believe parity is unlikely unless Germany's election results are unexpectedly disruptive. In GBP/USD, we expect support at 1.2200, while USD/JPY gains should be capped at 158.00. For USD/CNH, key resistance is at 7.3500, a level that may be tested but should ultimately hold.

Elsewhere, the Canadian dollar looks particularly vulnerable as the Bank of Canada's dovish stance adds to its headwinds. As for gold, the month-end price of $2,817 places it in overbought territory. The Relative Strength Index (RSI), a key technical indicator, suggests exhaustion, signalling a potential correction. From a technical perspective, once a downward move begins, we expect $2,720 to be the first target followed by $2600.

January performance vs. USD (%)



Source: CAIM, January 2025.

EQUITIES

SIMON PRICE

SENIOR EQUITY FUND MANAGER

United States

A positive month despite the increased questions

US equity markets reached new highs within the month, driven by a still-strong growth story, a soft CPI print, and early optimism surrounding the quarterly earnings season, which reinforced the Goldilocks narrative. However, several factors raised questions about the market gains, including a significant bond sell-off early in the month, though that later unwound due to softer inflation prints. Additionally, a separate risk-off move occurred due to DeepSeek's new AI model, which raised concerns about the sustainability of US tech valuations. While this too mostly unwound, it highlighted how dependent global equities are on a narrow group of stocks. Finally, tariffs resurfaced as an issue, with markets losing ground toward the end of the month after the new Trump administration announced plans to impose tariffs on Canada, Mexico, and China.

Turning to monetary policy, the FOMC, as widely expected, kept the federal funds rate unchanged in the 4.25-4.50% range after delivering 100 basis points of cuts over the previous three meetings. The session that followed saw mixed signals, with hawkish adjustments in the press release, notably removing the wording that "inflation has made progress toward the 2% objective." However, Chair Powell later downplayed this change, describing both the policy stance and the economy as being in a "good place." On the immediate signal, Chair Powell appeared to downplay the likelihood of a rate cut in March, although he noted that the policy stance remained "meaningfully restrictive."

The macro picture remained solid, with the latest US jobs report showing a larger-than-expected payrolls figure and the unemployment rate falling by a tenth to 4.1%. Regarding inflation, the core US CPI came in lower than expected, rising by only +0.2% month-on-month in December. However, the overall inflation picture wasn't ideal, as the headline CPI print reached a 10-month high. In the PPI release, while the main numbers surprised on the downside, it was clear upon closer inspection that components feeding into the PCE (the Fed's target measure) remained more robust.

Support for equities continued from the corporate earnings picture, with 4Q24 results now about halfway through. Financials showed strength, with net interest income up quarter-on-quarter at most banks, and moderate loan growth driven by C&I loans and credit cards. Investment banking and trading revenues were strong for capital centres, though core expense growth rose modestly, and capital ratios declined slightly, with share buybacks at nearly all banks. In technology, results have been mixed. Microsoft's shares fell despite a headline earnings beat, as cloud revenue growth missed estimates due to capacity constraints in the company's data centre business. Meta reported a solid earnings beat, but its Q1 sales guidance of $39.5bn to $41.8bn came in at the lower end of expectations. Tesla initially slipped after missing Q4 revenue estimates, but Elon Musk reassured investors by projecting "epic" growth and a return to positive sales growth this year. Apple delivered a marginal earnings and sales beat, with disappointing iPhone sales and China revenues offset by strong growth in the services division. Overall, investors seemed reassured by guidance indicating low-to-mid single-digit revenue growth in the coming quarter.

In terms of performance, major indices advanced, with strong market breadth at the sector level. The broadening theme continued, with Communication Services performing the best, while Healthcare and Financials also saw gains. Information Technology, however, struggled, with concerns about the sustainability of valuations in the sector following the DeepSeek news. Nvidia experienced the largest one-day decline in value, erasing $593 billion during the month.

Europe

Europe perhaps benefiting from US equity market questions

European equity markets extended December's gains in January, despite signs of economic stagnation in Q4. The rally was driven by a positioning/mean reversion story, some indications of political stability in France, dovish ECB signals, and a solid start to earnings season.
The ECB cut rates by 25bps to 2.75%, marking a total 125bps reduction since June. Further cuts are expected, though President Lagarde avoided specifying an endpoint.

Corporate earnings remain in early stages, but consumer sector pre-releases exceeded expectations. The major indices saw strong relative outperformance with cyclicals outperformed defensives, as luxury stocks rallied despite China-related concerns from LVMH. Banks gained on strong U.S. earnings and M&A activity, while EU defense stocks benefited from rising NATO spending expectations. However, semiconductor and electrification sectors were pressured by DeepSeek-related headlines.

Developed Asia

Muted tariff impact aids HK, while BoJ actions a hurdle for Japanese equities

Developed Asian equity market performance was mixed with Hong Kong seeing gains on less-than-feared initial US-China tariff tension while Japanese markets consolidated/saw slight losses as the BoJ have raised rates to 0.5%.

Japanese equities had a slow start in January, with TOPIX up just 0.1% and the Nikkei 225 down 0.8%. Early gains, driven by foreign demand stocks amid yen depreciation, reversed mid-month after BoJ officials signalled a hawkish stance, sparking futures-led selling, on concerns of a replication of a huge but brief global sell-off in July of last year. After markets digested the BoJ's rate hike, semiconductor stocks were hit by the DeepSeek shock, followed by Trump's tariff announcement. However, Japan may be less impacted by U.S. tariffs due to efforts to manage its trade surplus and increase U.S. investment.

Emerging markets

EM equities posted modest gains in January, underperforming developed markets. Risk assets benefited from positive developments, including a weaker USD, but the late-month announcement of new U.S. tariffs on Canada (25%), Mexico (25%), and China (additional 10%) weighed on sentiment. The USD weakened through most of the month.
Regionally, LatAm and CEEMEA outperformed, while EM Asia lagged.

AUTHORS

Charles Thomson
Head of Portfolio Management
charles.thomson@caiml.com

Slawomir Soroczynski
Head of Fixed Income
slawomir.soroczynski@caiml.com

Simon Price
Senior Equity Fund Manager
simon.price@caiml.com

CONTACT

Crown Agents Investment Management
The Rex Building
62 Queen Street
London
EC4R 1EB
United Kingdom

www.caiml.com
CAIMInsights@caiml.com
T: +44 (0)20 7489 7223

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