Amplia Monthly Investor Letter

The Dance of Uncertainty

As the year drew to a close, markets found themselves in a delicate choreography of anticipation and reaction. Each step, whether from policymakers, investors, or economic indicators, influenced the rhythm of global financial performance. December was no exception, as a complex interplay of optimism, caution, and evolving dynamics set the stage for the coming year.

Market Performance: December Highlights

The final month of 2024 ended on a generally disperse note for equities. U.S. markets suffered from continued inflationary pressures, with the S&P 500 shedding a bit. European equities, lagging behind their U.S. counterparts, were down a little bit more. Bond markets were broadly in the red, with U.S. Treasury yields edging higher on expectations of limited rate cuts in 2025, while European yields rose due to mounting inflationary pressures.

31.12.2024				
Equities	Currency	Return mtd (eur)	Return ytd (eur)	Return 12m (eur)
World	USD	-0,5 %	0,0 %	18,7 %
Emerging Markets	USD	2,0 %	0,0 %	7,5 %
US	USD	-0,3 %	0,0 %	24,5 %
EU	EUR	-0,5 %	0,0 %	8,8 %
UK	GBP	-0,9 %	0,0 %	9,7 %
Japan	JPY	1,7 %	0,0 %	20,6 %
South-Korea	KRW	-5,6 %	0,0 %	-9,9 %
China	USD	1,8 %	0,0 %	14,5 %
Finland	EUR	-0,4 %	0,0 %	-4,7 %
Sweden	SEK	-0,6 %	0,0 %	3,9 %

Bonds	Currency	Return mtd (eur)	Return ytd (eur)	Return 12m (eur)
Euro Government	EUR	-1,3 %	0,0 %	2,0 %
US government	USD	0,6 %	0,0 %	0,6 %
Europe IG	EUR	-0,4 %	0,0 %	4,1 %
US IG	EUR	-2,7 %	0,0 %	-0,7 %
EU HY	EUR	0,6 %	0,0 %	8,2 %
US HY	EUR	-0,6 %	0,0 %	6,4 %
Emergin Markets HC	EUR	-1,4 %	0,0 %	4,7 %
Emergin Markets LC	EUR	0,9 %	0,0 %	7,6 %

Equity and bond returns. Source: Bloomberg, Amplia.

U.S. equities were flat in in December euro terms (-0.3%) but declined in dollar terms (-2.7%). Emerging market stocks outperformed with a return of 2.0%. Bond markets faced a challenging month, struggling with the impact of higher expected central bank rates and rising inflationary pressures.

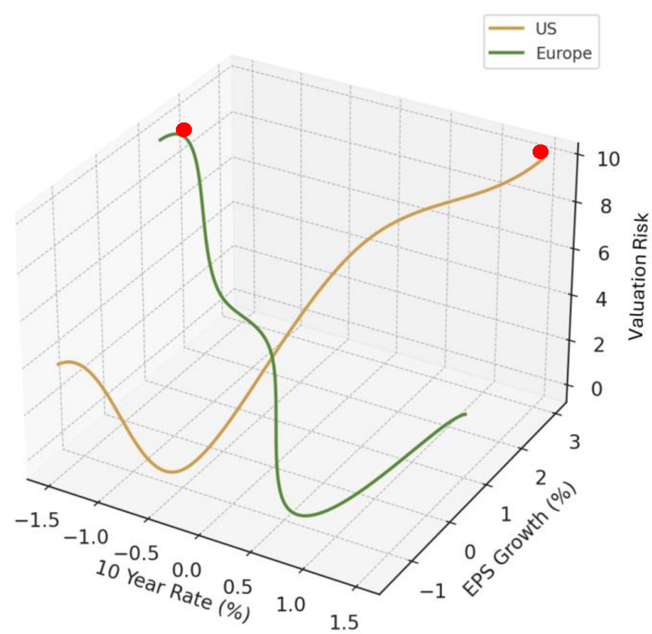
Macro: Crosscurrents Shaping the Global Economy

The Federal Reserve's December commentary marked a pivotal shift in market expectations, with participants now pricing in only two rate cuts for 2025. Despite elevated policy rate expectations, monetary conditions in the U.S. remain loose, providing additional support to the markets. Notably, the Federal Reserve's assessments seem to overlook the potential productivity gains stemming from artificial intelligence, a factor that could introduce upside risks to 10-year Treasury rates through overheating, even though a leap in productivity itself is deflationary. Further bolstering the U.S. economic outlook are Trump's proposed measures, including tax cuts, import tariffs, and heightened activity in energy sectors such as drilling and fracking. However, with a divided Congress also within the Republican Party, these initiatives face the risk of delays or dilution.

In Europe, the economic landscape is dominated by chronic low growth, exacerbated by upcoming elections in Germany and France. Budgetary constraints stemming from defense spending, climate change initiatives, and aging populations add further pressure, leaving scant room for fiscal flexibility. Downward pressure on European interest rates seems inevitable. Nonetheless, the environment remains supportive of low but gradually improving growth.

Valuation: Navigating Tight Space

Valuations across global equity markets continue to appear expensive. Investor attention is firmly fixed on the impact of interest rates, where risks lean bearish, and on potential productivity and growth enhancements, where the risks are bullish. The wide interest rate differential between the U.S. and Europe bolsters the case for European equities' relative outperformance. The dynamics of rates and growth highlight stark differences between the two regions. In the U.S., valuation risks peak when rates rise alongside growth, creating overheating concerns. Conversely, in Europe, falling rates pave the way for stronger earnings-per-share growth, with valuation risks emerging when lower rates spur excessive growth—an effect largely driven by duration risk.

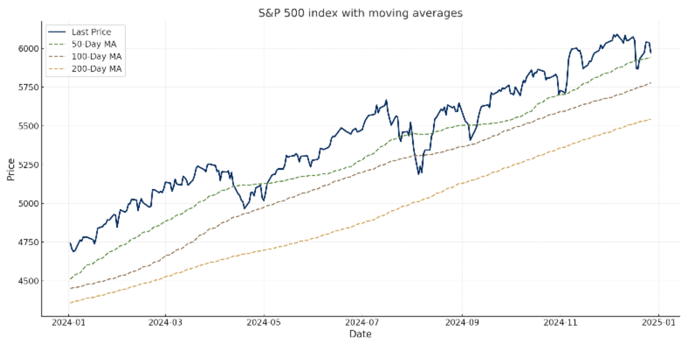


Source: Amplia

The graph illustrates the valuation risks in Amplia's scenario analysis. The highest risk scenario in Europe occurs when EPS growth increases and interest rates decrease, whereas the riskiest scenario in the U.S. is a high-growth, high-interest-rate environment.

Sentiment: Optimism Tinged with Caution

December's sentiment reflected a balance of optimism and caution. After a brief surge in risk premiums, with the VIX index jumping from 15 to 27, volatility metrics returned to normal levels by month-end. Investors appear keenly focused on technical levels, with the 50-day moving average acting as a critical support threshold, attracting bargain hunters as prices approach this level. Should this threshold be breached meaningfully, the gaps to the 100-day and 200-day moving averages—at 3.4% and 7.2%, respectively—become increasingly relevant. Provided no significant negative shocks occur (unknown unknowns) and as long the VIX does not remain above 25% for extended periods, positive sentiment is likely to persist. The "musical chairs" dynamic of market momentum continues to keep participants engaged and optimistic.



Source: Amplia, Bloomberg

Asset Allocation: Balancing Caution and Opportunity

In light of these developments, we remain cautiously optimistic and maintain an overweight in equities. Within portfolios, we are contemplating adding defensive equity risk, targeting sectors less exposed to long-duration interest rates in the U.S. while capitalizing on Europe's potential for earnings growth. In fixed income, we are considering reducing exposure to long-duration U.S. bonds to mitigate the impact of rising yields, focusing instead on intermediate maturities. Geographically, we are cautiously increasing our assessment of European equities, given their valuation appeal and narrowing gaps relative to the U.S., while remaining vigilant about potential disruptions stemming from global trade and U.S. policy shifts.

As we enter 2025, the intricate interplay of growth, policy, and sentiment will continue to shape the market landscape. We might be in the coda section of the symphony of our musical chairs game, but as professional players, we aim to read a few bars ahead in the script, seeking opportunities to enhance long-term portfolio performance.

On 2nd January 2025,

Yours sincerely,

Mikael Simonsen