2025 Market Outlook

As the world continues to undergo a structural transformation, redefining economies and investment approaches, we continue to see opportunity in developed equity markets, notably the United States (US). However, global markets are more sensitive this year, making a granular and dynamic investment approach key. The case for a tilt to emerging markets (EM) grows.

Since the end of the ultra-loose monetary-policy era and benign inflation marked by the COVID-19 pandemic, Cogence and its partners have maintained that the world is undergoing a structural transformation, reshaping economies.

This seismic transition – rather than a normal business cycle – has spurred global equity markets over the past two years. We see this momentum continuing into 2025, notably in the US.

However, the system is more sensitive than in 2024. Several factors could shift the outlook:

Global policy shifts, many of which elevate inflation as new leaders take the stage during a time of geopolitical conflict; a change in investor sentiment as we await earnings data; and the potential for a jump in bond yields given rising term premiums in the US.

"There is some uncertainty this year, definitely more than last year," says Jonel Matthee-Ferreira, CEO and CIO of Cogence. "We are pro-risk to US equities in the short term, but that can change tomorrow, and we need to be able to react. This is why we believe a dynamic, granular portfolio, leveraging active and passive strategies, will be critical for the year ahead."

"Another important element, we believe, is that portfolios need to be more tactically aligned to thematic issues – the mega forces reshaping the world."

Beyond developed markets, 2025 may prove to be a pivotal year for emerging markets too.

The views expressed are based on information available as of 10 February 2025 and may be revised as market conditions change.

The year **that was**

In 2024, the US enjoyed a second year of positive momentum, as strong economic performance, an accommodative fiscal environment and significant private spending through the capital markets supported investor interest in the transformative potential of artificial intelligence (AI). US equities, as measured by the MSCI USA Index, returned 25% (USD) after a 27% gain, yet again defying predictions of slower growth – or a 'hard landing'.

Appropriately diversified global investors have fared well.

The performance once again supports BlackRock's view, adopted since 2020, that we are not in a normal environment. If this was business as usual, then tighter financial conditions should have slowed growth while bringing down inflation.

Instead, inflation has eased, but growth has not.

"Economies are undergoing a transformation that could keep shifting the long-term trend, making a wide range of very different outcomes possible," says global asset manager BlackRock[1].

This transformation – driven by era-defining mega forces such as AI, decarbonisation, ageing populations and significant public and private spending in these areas – has motivated investor interest in AI, supporting returns in US tech giants, despite elevated valuations.

Locally, South Africa enjoyed one of its best years on record, with both the local fixed-income and equity markets experiencing a substantial rally.

The FTSE/JSE All Bond Index (ALBI) delivered one of its highest calendar-year returns, registering a solid + 17,2% (ZAR), while the Small Cap Index delivered an exceptional 35,6% (ZAR) and property 29,8% (ZAR). From a fixed-interest market perspective, yields declined across the duration spectrum, with the long-dated R2,048 sovereign bond declining from over 12% (ZAR) at the start of 2024 to 11% (ZAR) by year-end.

The turnaround was triggered by investors' positive sentiment towards the formation of the Government of National Unity (GNU), a resilient currency in the face of dollar strength and an easing of inflation.

According to an analysis done by RisCura, we are entering what may be a pivotal year for emerging markets, which may deliver meaningful growth in 2025. South Africa, once known for its volatility and risk as an emerging market, is now gaining favour among investors due to a unique local narrative and limited alternatives in the emerging market universe.

[1]BlackRock | 2025 Global Investment Outlook: Building the transformation, 4 December 2024

The global year ahead

Going into 2025, Cogence and BlackRock, which manages the asset allocation and global manager selection of our investment solutions, continue to see potential in developed market equities.

Growth is anticipated to continue to broaden beyond the US tech giants to companies and sectors that sit at the crossroads of the era-defining mega forces, which have the potential to outsize the Industrial Revolution in terms of their breadth and impact on the composition of economies.

AI holds the potential to improve productivity and accelerate the pace at which ideas are generated, spurring innovation and fundamentally reshaping industries. BlackRock sees spending in the current buildout phase of the AI transformation potentially topping $700 billion by 2030, equivalent to 2% of US GDP. However, the trajectory of the eventual transformative promise of AI remains uncertain. At present, we are in the buildout phase of the AI evolution, as tech companies race to build the infrastructure AI needs. In phase 2, the adoption phase, applications mature and adoption is likely to accelerate as AI is packaged into different apps and software.

Finally, in the transformation phase 3, companies could unlock the full value of AI adoption as broad productivity gains and new business models and industries emerge.

The energy transition – intertwined with mega forces like AI and geopolitical fragmentation – is also spurring major innovation and investment. Conversely, ageing populations[2] in major economies constrain labour supply, which could limit how much countries can grow. However, some emerging economies may benefit from younger populations and growing middle classes.

“As we argued last year, these forces are reshaping the composition of economies, permanently shifting long-term trends,” says Matthee-Ferreira. “Markets are realising that we are not in a normal business cycle.

“We continue to be overweight to US equities as they stand to benefit the most from mega forces, but also as growth is still positive, there are tax cuts potentially coming through, and there might be some regulatory easing under Donald Trump.

“Mega forces should be positive for corporate earnings, but we see this occurring in slightly different avenues than last year as growth broadens beyond tech stocks to sectors such as energy, infrastructure, and healthcare.”

[2]BlackRock Investment Institute | Demographic Divergence, March 2024

Positive, but **less certain**

The recent rally in US markets, fuelled by investor interest in AI and supported by robust corporate earnings, technological innovation and substantial private sector investment, comes off a high base, following more than a decade of US outperformance relative to the world. The US equity market now constitutes around 75% of the MSCI World Index, which tracks the performance of 23 developed markets, highlighting how quickly markets and economies can be transformed by the era-defining influence of mega forces.

BlackRock argues that valuations, with the S&P 500 now trading at multiples in the region of 25 times earnings, may not tell the full story of the equity market's changing compositions as economies are reshaped. Valuations are also more relevant for long-term performance and less so in the short term.

However, the price of US stocks relative to history does raise the risk that markets could turn frothy if tech earnings underwhelm, especially considering the enormous private sector investment in mega-tech-related research and infrastructure, such as data centres.

"While earnings might surprise the upside, any misses could renew investor concern over whether big AI capital spending will pay off and if high valuations are justified – even if we think valuations can't be viewed through a historical lens as an economic transformation unfolds," says BlackRock[3].

There is also some ambiguity around the impact of new leaders, such as Donald Trump, who may affect inflation while elevating geopolitical trade tensions. While Cogence is pro-risk US equities, this does not extend to treasuries as a potentially growing budget deficit adds to ongoing fiscal pressures in the US.

The atypical environment challenges long-standing assumptions about how to build portfolios, including the neutral 'benchmark' portfolio, which consists of equities and bonds in a traditional 60/40 mix.

"We could go in a lot of different directions this year and it's essential to get granular while remaining responsive to any shifts in the outlook. At Cogence, we update our portfolios monthly or intra-monthly when required as we adapt to this fast-changing environment," says Matthee-Ferreira.

Beyond the US, Japan appears to be undergoing a significant turnaround marked by a much-needed uptick in inflation, driven by wage growth and supported by a combination of fiscal and monetary policies aimed at stimulating demand, as well as structural reforms to enhance corporate governance and efficiency – a development noted by BlackRock.

While opportunity abounds in developed markets, heightened valuations in developed countries could strengthen the case for emerging markets.

"In the shorter term, from a dynamic, tactical perspective, we are very much risk-on, US-focused. In terms of our longer-term strategic asset allocation, we do favour emerging markets and South Africa will be very interesting," says Matthee-Ferreira.

At the start of 2025, Cogence was overweight in US and Japanese equities and overweight in SA bonds.

[3]BlackRock | Triggers to change out pro-risk view, 13 January 2025

An **emerging story**

"In our view, it is a pivotal time for emerging markets (EM) as the rate-cutting cycle in the US has begun," says Matthee-Ferreira. "This dynamic could benefit EM by widening the interest-rate differential in favour of EM assets."

While the Federal Reserve cut rates in 2024, the extent of the cycle was less than the market had predicted and in line with our view. Further, strong US economic data, structural pressures driven by mega forces, and rising protectionist trade policies – particularly in the US – suggest that inflation will likely remain elevated above pre-COVID-19 levels for longer. This could limit the speed and magnitude of interest-rate cuts in the US, constraining the extent of monetary easing globally.

It remains prudent to maintain some exposure to the US, given its status as an advanced economy and its global influence. However, selective emerging markets offer compelling investment opportunities, with attractive valuations and stronger earnings prospects. These markets provide access to diverse economies with unique growth dynamics, creating the potential for competitive returns.

Consensus earnings per share growth forecasts %

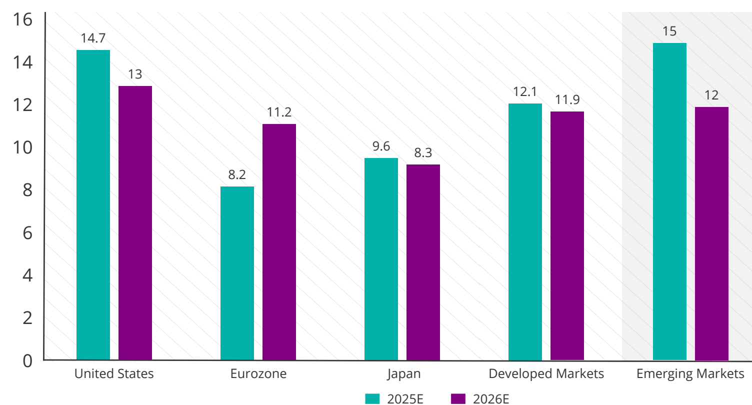


Chart 1: Consensus earnings per share growth forecasts, (Source: Alliance Bernstine)

However, as Cogence reaffirms the need for investors to rethink paradigms, country-specific granularity for EM is key. BlackRock sees those EM regions at the crosscurrents of mega forces, such as Saudi Arabia and India, as attractive.

Meanwhile, countries in the firing line of Donald Trump's proposed protectionist trade policies, such as Mexico and Vietnam, may be at risk of subdued performance. In contrast to EM countries with the largest trade surpluses with the US, South Africa's surplus is less than 2% of GDP.

It remains critical for South Africa to navigate its trade relationship with the US carefully and to remain in the African Growth and Opportunity Act (AGOA).

Goods trade surplus with US (%GDP)

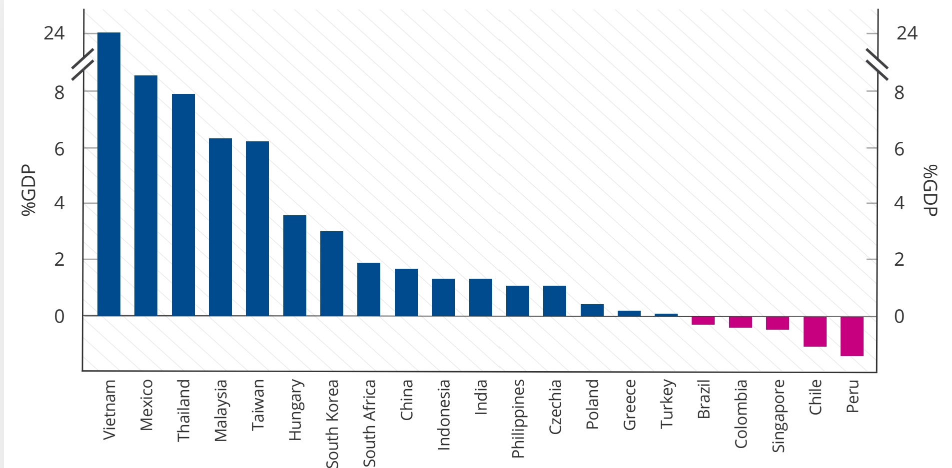


Chart 2: International trade surplus with the (US Source: IMF Dots, Alpine Macro)

A spotlight on **South Africa**

"While many are undervalued from an equity market and currency perspective, these markets require a closer look for investment opportunity. We think SA is one of those markets where the valuation does support the opportunity. SA equity markets have had a strong rally but still show value with foreign investors not yet having made big moves into the market," says Matthee-Ferreira.

"South Africa has long grappled with a reputation for volatility and risk as an emerging market (EM), further exacerbated by its greylisting in 2023 and ongoing corruption issues," says RisCura[4].

"However, a turning point has been reached. The country is now emerging as an EM favourite among investors due to its unique local story and the shortage of alternatives in the EM universe. Recently, S&P upgraded the country's credit outlook to positive, reflecting investor confidence around the formation of the Government of National Unity (GNU), a coalition between the ANC, DA and IFP."

Encouragingly, the National Treasury reports that 16 out of the 22 issues highlighted by the Financial Action Task Force (FATF) have been mostly or fully resolved, signalling progress on the greylisting status. Further, inflation has been moderating, creating room for the South African Reserve Bank (SARB) to continue to cut interest rates despite some conservatism at the national treasury.

South Africa's rate of inflation has come down from 7,9% to just 2,9% – below the lower bound of the SARB's target range of between 3% - 6%. "This marks one of the most notable success stories in the EM world over the past two years," Matthee-Ferreira says. However, there are ongoing discussions around what the inflation-target boundaries will be going forward as the SARB called for a review of the country's target range in October 2024. If the inflation target is revised downwards to be more in line with EM peers, it could face opposition from labour unions and policymakers concerned about the potential impact on economic growth, particularly in an environment already grappling with high unemployment and income inequality. This could have a knock-on effect on the fixed-interest market.

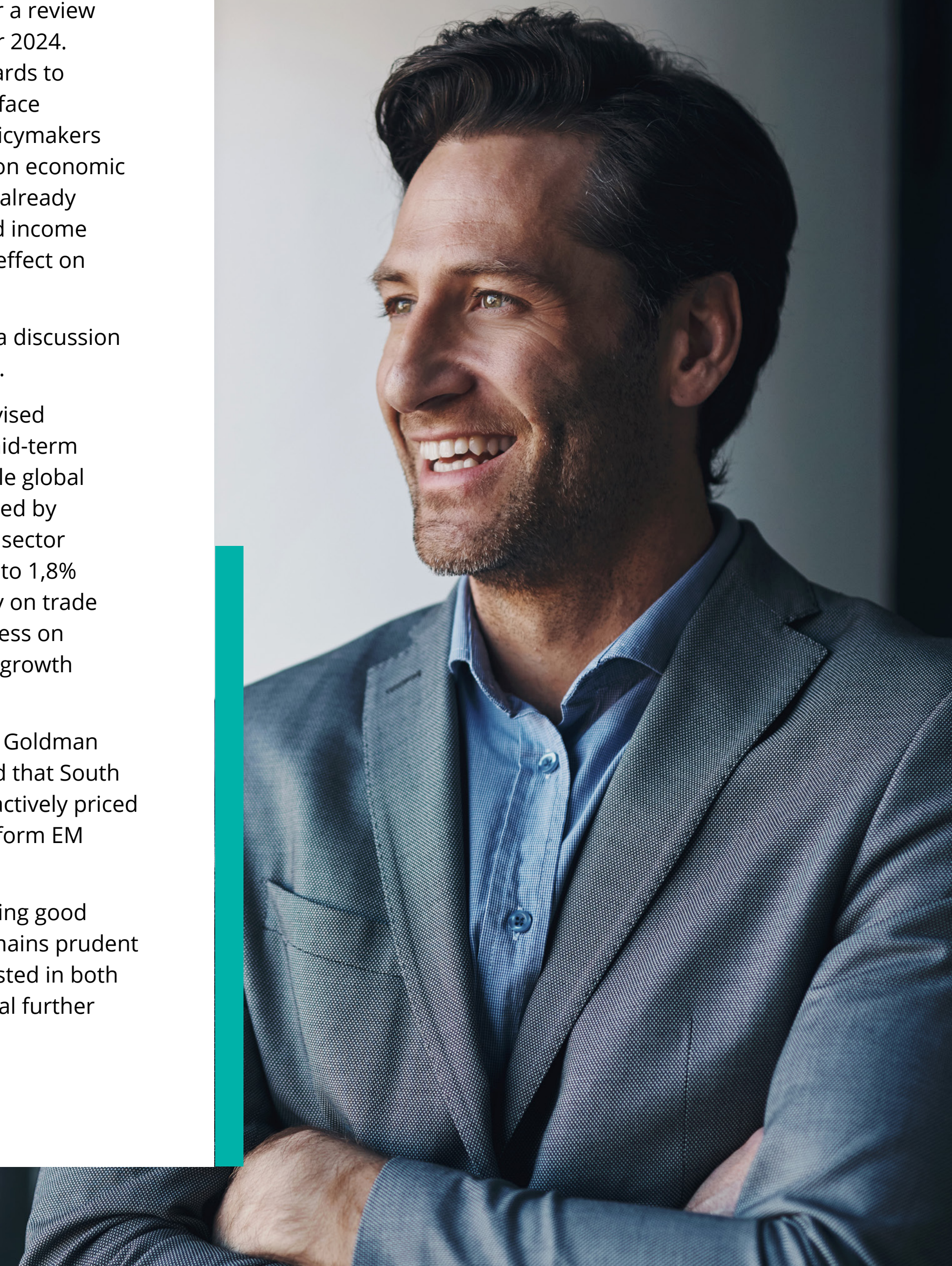
These factors, ultimately, boil down to a discussion about economic growth in South Africa.

Although growth expectations were revised downwards from 1,3% to 1,1% in the mid-term budget policy assessment, a more stable global environment going into 2025 – supported by local factors such as private and public sector collaboration – has seen this projected to 1,8% between 2025 and 2027. Greater clarity on trade relations on the global stage and progress on local reforms will be crucial to manage growth expectations going forward.

Leading financial institutions, including Goldman Sachs Group and Société Générale, said that South Africa's undervalued currency and attractively priced equity and bond markets could outperform EM peers in 2025.

"With both SA equities and bonds offering good value and screening as attractive, it remains prudent for South African investors to stay invested in both these areas to capitalise on the potential further upside," concludes Matthee-Ferreira.

[4]RisCura | Market Outlook 2025, 15 January 2025



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Note: Past performance is not an indicator of future performance.

Source: ***BlackRock Investment Institute | 2025 Market Outlook, 31 December 2024***

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