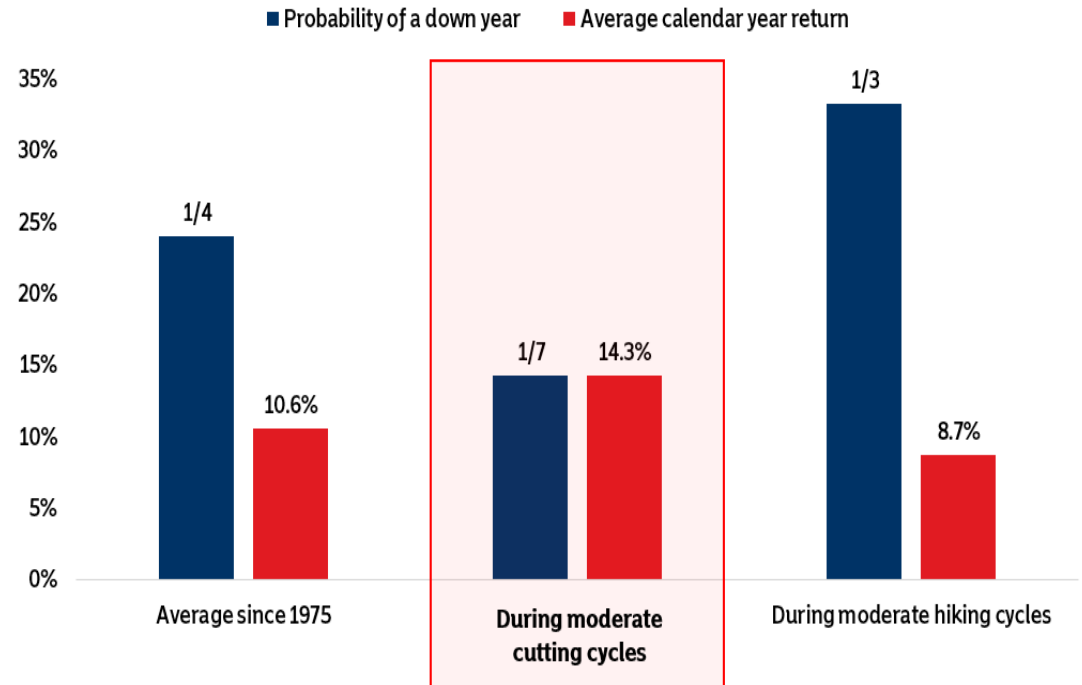


Equities like cutting cycles

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Source: Momentum Global Investment Management, Bloomberg Finance L.P. Data to 31 December 2024.

What this chart shows

This chart supports what we know: that equities like interest rate cutting cycles. Looking back at the past 50 years of the Fed funds rate and the S&P 500 Index, we find that calendar years during which interest rates drifted down by up to 1% were positive for the market. During these moderate cutting cycles, the chance of a negative year for the index fell from 1 in 4 years to 1 in 7, and the average return of the index (excluding dividends) increased by roughly 4% to 14.3% per annum. This idea is reinforced by looking at the alternative scenario: during moderate hiking cycles, chances of a negative year increase to 1 in 3 and average returns drop by close to 2%.

Why this is important

Inflation, while less talked about of late, remains critical to the outlook for markets from here. If inflation remains under control, then there's every chance that fairly orthodox monetary policy – i.e. a moderate cutting cycle – can be used to steer a smooth path for economies, and in that environment the majority of investments should do well.

We should remember that the prospect of a continued moderate cutting cycle provides a powerful underpin to equities, outside of the most extended parts of markets today. But we should also keep in mind that, like any rule, this one is not perfect – in 1990 for example, the Fed fund rate was cut by a percent and yet the S&P still fell -7%. One should therefore continue to look at a range of inputs when deciding how to position portfolios today.



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