Market Weekly Insights

3rd February 2025

S&P 500	$6,040.53 -0.50%
DJIA	$44.544.66 -0.75%
NASDAQ	$19,627.44 -2.24%
Russell 2000	$2,303.84 -1.42%
FTSE 100	$8,673.96 +0.31%
Nikkei 225	$38,728.36 -2.20%
WTI Crude	$73.82 +1.75%
10-yr Treasury	4.525%

Global Outlook

Market Concerns Growing Over Germany's Economic Model

Germany, home to the world's third-largest economy, is facing significant challenges posed by their export-driven economic model. The rise of luxury Chinese automobiles offered at more competitive prices than German competitors has led to China's automobile industry grabbing significant market share both in China and on the global market, at the cost of Germany's. Specifically, Germany's industrial output has decreased by 15% since 2018 with employment in the manufacturing sector down 3% as well. The core issue Germany is facing is the changing reality that the world has turned to alternative products than those made in Germany

For decades, the German government has subsidized export manufacturing, often at the expense of investment in emerging sectors such as IT and AI. The country's exports as a percentage of GDP are almost four times the U.S.'s share and twice China's. Combined with a coalition government collapse, Germany faces a tough question as to how it can diversify economic output on a global scale to compete with rising and established economies. While the automotive industry remains Germany's strongest, both corporations and governments alike are pressed as to whether they should consider changing their economic model entirely, which is already posing significant ramifications in global markets.

DeepSeek Disrupts Global Markets and Redefines Macroeconomics

DeepSeek's newly released large language model (LLM) took the world by storm this week, with the NASDAQ down over 3% shortly after its release. Notably, Nvidia's stock price dropped nearly 17%, one of the largest single-day losses for the world's leading semiconductor company, as financial markets grappled with idea that a Chinese competitor developed a highly efficient LLM with inferior chips at the fraction of the price of its American counterparts. Although Wall Street analysts have expressed optimism about the rebounding of semiconductor companies, one of the key component's in DeepSeek's LLM was its fully open-source platform.

By creating an open-source platform, DeepSeek has circumvented the US Semiconductor export ban and opened their product up to the global market. Software companies and engineers will be able to access DeepSeek's open-source platform for a minimal cost, meaning the new focus for the semiconductor and data center industries has shifted from scalability to efficiency. Additionally, investors have expressed concern that chipmaking equipment manufacturers such as ASML and energy companies could see reduced growth as DeepSeek's launch, has stalled the scalability of data centers and semiconductor manufacturing. Looking forward, both software and manufacturing companies alike have already started shifting their attention to efficiency amongst chips and the quality of LLM's themselves.

Sources: Newsweek, Yahoo Finance, Reuters

Czech Central Bank Weighs Bitcoin for Reserves

The Czech National Bank (CNB) is considering adding Bitcoin to its foreign exchange reserves, with Governor Aleš Michl proposing an allocation of up to 5% of the country's €140 billion holdings. This could mean an investment of approximately €7 billion in cryptocurrency. Michl argues that Bitcoin's growing acceptance, particularly through exchange-traded funds (ETFs) from major financial institutions, makes it a valuable diversification tool. Despite its volatility, he believes its long-term potential could justify its inclusion in the country's asset portfolio.

However, the proposal has been met with skepticism from European financial authorities. The president of the European Central Bank (ECB), Christine Lagarde, dismissed the idea, emphasizing that central bank reserves must remain stable and liquid—qualities Bitcoin lacks due to its price swings and concentration among a limited number of holders. Other central banks in the region, including those in Poland and Romania, have also stated they have no plans to incorporate cryptocurrencies into their reserves. The CNB is expected to continue evaluating its reserve management strategy before making a final decision; if they decide to go ahead with it, then the Czech Republic will be the first Western European nation to integrate Bitcoin into its central bank reserves.

Record £2.2B Retail Theft Prompts Calls for Stronger Measures in the UK

Despite a £1.8 billion investment into security for retail stores, the British Retail Consortium (BRC) reported that retail crime had reached record levels with theft resulting in losses of £2.2 billion in a single year, an increase of £400 million from the prior year. Additionally, the report indicated that 2000 violent incidents were committed against retail staff on a daily basis back in 2020/2021 due to a lack of police attendance.

The Co-operative Group, a group of individuals close to businesses, launched Project Pegasus in late 2023 to lessen these crimes. Since the project's inception, there have been many positive impacts, such as increased police attendance from 20% to 66%, and developments in AI technologies to detect concealed goods and physical assaults better. To further lessen the impact of these crimes, the BRC continues to push for initiatives such as removing the £200 threshold that classifies thefts as low-level and creating a new offense for assaulting retail employees.

America This Week

December Sees Surge in New Home Sales

The U.S. Census Bureau reported that in December 2024, the sale of single-family homes increased by 3.6% beating expectations, and leading to the seasonally adjusted annual rate from December increasing to a projected 698,000 units. This represented a 2.5% increase in new homes sold year-over-year, with the median house price increasing by 2.1% to $427,000. While high mortgage rates have created pressures on the housing market, new home sales continue to outperform existing home sales primarily due to greater supply.

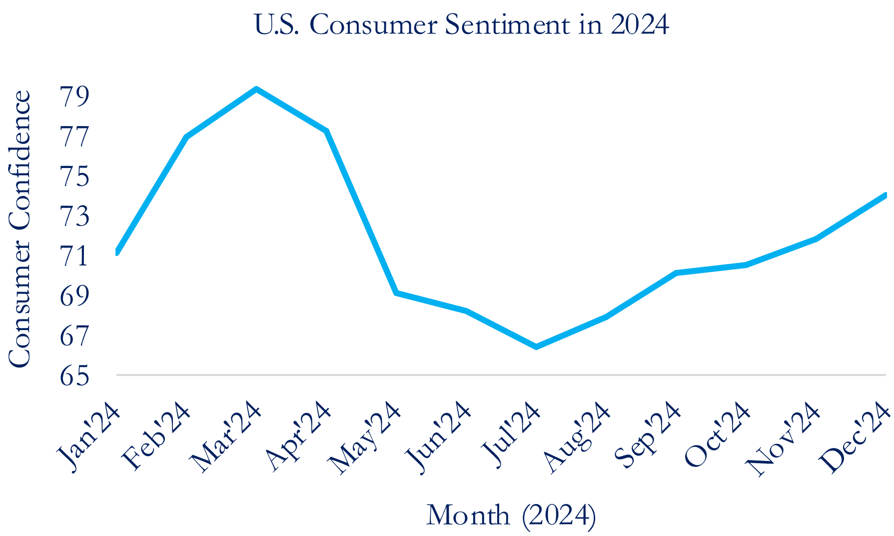
Sources: Reuters

The increase in the sales of new homes differed vastly by region, with home sales increasing in the Northeast and West by 41.7% and 20.3%, respectively, whilst sales decreased in the South and Midwest by 2.1% and 3.3%, respectively. With the increases in these sales, inventory for new homes reached 494,000, the highest number since December 2007. This increase in inventory has a projected 8.5-month supply, showing a potential oversupply. Economists are projecting that the rise in new home sales will continue compared to existing homes due to its higher availability.

U.S. Consumer Sentiment Declines in January; Inflation Expectations Rise

In January, the University of Michigan's consumer sentiment index decreased to 73.2 from December's 74.0, indicating a slight decline in consumer confidence mainly due to the worries about the labor market and the tariffs on imports that have been speculated to be implemented in the coming months. Despite the consumer confidence dip, however, the index remains above the 2024 average, suggesting that consumers are still relatively optimistic about the economy.

The same survey further revealed that consumers' 12-month inflation expectations have risen to 3.0% from 2.9% in December. Additionally, almost 50% of consumers expect unemployment to rise in the year ahead. This therefore reflects growing concerns about potential price increases in the near future. Economists monitor these expectations closely, as they can influence actual inflation if consumers adjust their spending behaviors accordingly.



Gold Liquidity in UK Significantly Affected by Mass Bullion Shipment to the US

The US market sentiment over the last few months has been speculative and defensive towards the impacts of potential tariffs implemented by the new administration. Commodity traders and financial institutions have been acquiring $82bn of bullion from the Bank of England in the last two months, lowering gold liquidity in the U.K. to an all-time low. The wait to withdraw bullion rose from a few days to between four to eight weeks, as the central bank struggles to keep up the demand.

Sources: Reuters, Financial Times

With uncertain trading policy, many industry insiders are operating on the assumption of potential tariffs on imported raw materials coming into the US. The vaults of the Comex commodity exchange have experienced an increase in inventory levels of 75 per cent to 926 tones, which is the highest since the Covid pandemic. The shipments are driven by higher prices on the New York futures exchange compared to the London cash market. This rare arbitrage opportunity has encouraged traders to transport the metal across the Atlantic as they continue to increase gold stockpiles in the United States.

Macro Highlights

Record U.S. Goods Trade Deficit Likely to Impact Q4 GDP Growth

In December 2024, the U.S. goods trade deficit expanded to a record $122.11 billion, up from around $103.5 billion in November. This significant increase was primarily driven by businesses increasing imports of industrial supplies and consumer goods in anticipation of potential tariffs from the incoming administration. The widening trade gap is expected to negatively affect the fourth quarter's GDP growth. Data indicates that the U.S. economy grew at an annualized rate of 2.3% in Q4, a slowdown from the 3.2% pace observed in the third quarter. While consumer spending remained strong, the substantial trade deficit likely reduced the overall economic growth.

Economists caution that the record trade deficit could pose challenges for economic growth moving forward. The increase in imports, driven by concerns over potential tariffs, may lead to an imbalance that could weigh on future GDP figures. As the new administration's trade policies take shape, businesses and policymakers will need to monitor these developments closely to assess their long-term economic implications.

Fed pauses interest rate cuts, awaiting clarity in upcoming economic policies and data

Following the meeting last Wednesday, the Federal Reserve, led by chairman Jerome Powell, has decided to halt on further interest rate cuts, keeping the federal funds rate at 4.25 – 4.5% range and entering a cautionary phase as they await clarity on economic data and policies in the coming months. Even though inflation has slowly moved to its 2% target throughout 2024, inflation rose to 2.9% in December, largely due to higher energy and gasoline prices.

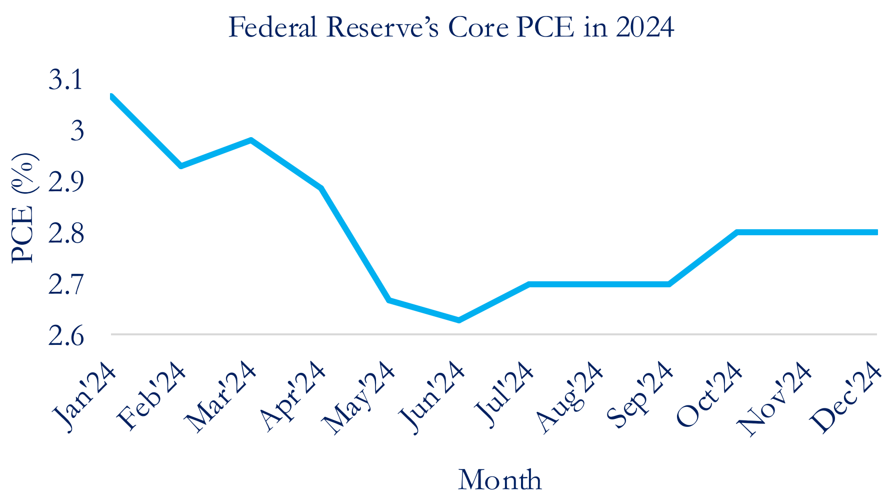
Sources: Financial Times, Reuters

Chair Powell stated that their next decision will be determined by Federal Reserve's favorite economic indicators like the CPI, PPI, and PCE, and how the market reacts to ongoing fiscal policies and global economic conditions. Powell emphasized that while the current interest rate level provides stability, the central bank remains flexible and will adjust its policy as needed. He reiterated that the Fed's primary focus is on achieving long-term price stability and maximum employment, which will guide their decisions in the upcoming Federal Open Market Committee (FOMC) meetings. With the next FOMC meeting scheduled in March, financial markets and policymakers will continue scrutinizing economic data, ensuring that any policy adjustments align with the Fed's dual mandate of price stability and full employment.

Federal Reserve's Core PCE Data in Line with Expectations

The personal consumption expenditure (PCE) price index increased 2.6% on a year-over-year basis in December, with core PCE coming in at 2.8%, which while in-line with expectations is still ahead of the Federal Reserve's 2.0% target. This increase in expenditures marked that inflation closed out 2024 still high and leaves a cautionary Federal Reserve heading into 2025.

The data comes out two days after the latest Federal Reserve meeting where they unanimously voted to hold interest rates. The Federal Reserve expressed a desire to see continuation in lower inflation levels before making any further decision on interest rate cuts. While food prices increased just 0.2% in December, energy prices increased 2.7%, an indication of high global demand stemming from the AI and data center race in addition to current geopolitical complications. However, the three-month PCE, is currently, 2.2%, down from 2.8% in the three months preceding October, providing the Federal Reserve with some positive data moving forward



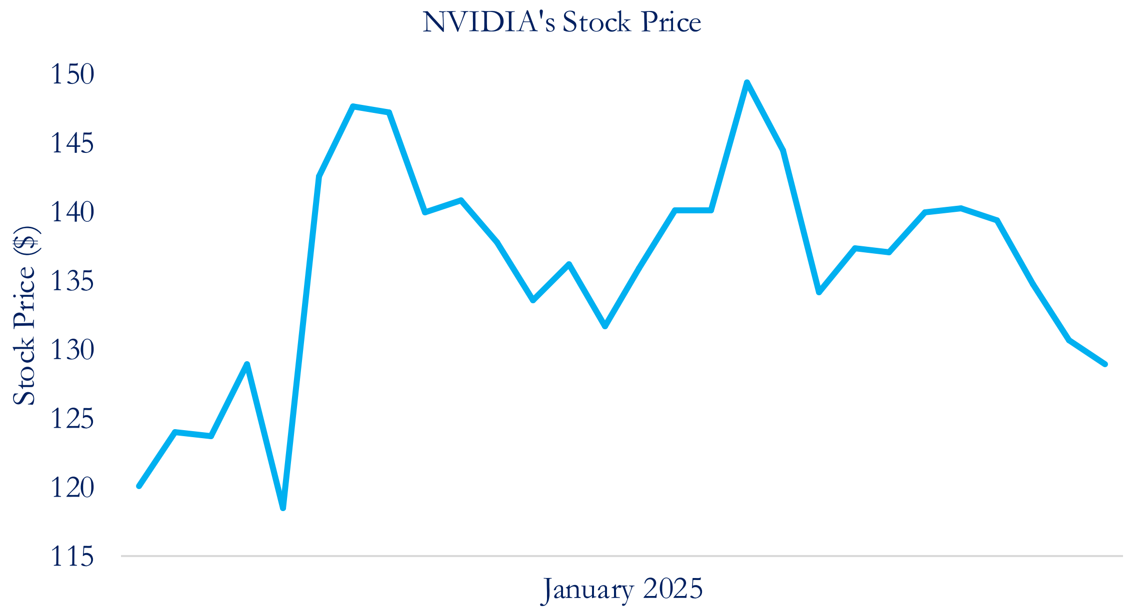
Industry News

DeepSeek's AI Breakthrough Wipes $600 Billion Off Nvidia's Market Value

Nvidia experienced its worst trading day since the 2020 pandemic sell-off last Monday. After the company Deepseek, a small Chinese company, released its R1 reasoning model challenging the likes of OpenAI, Nvidia's stock plummeted 17% in just one day, causing a loss of $600 billion in market value. Before this, Nvidia had been experiencing financial success, with revenue increasing 200% over the last two years to $126 billion and market value peaking at $3.62 trillion in November.

Sources: Wall Street Journal

Deepseek's breakthrough went beyond Nvidia; it also decreased the shares of many other semiconductor companies, such as Broadcom, Micron Technology, and Taiwan Semiconductor Manufacturing Inc. This new technology from Deepseek, with its main attractiveness being its cost-effectiveness, has challenged the prenotion that an increasing number of expensive Nvidia chips were needed for AI systems. The response seen in the market has indicated that AI chipmakers will now face additional pressure to innovate and create more cost-effective AI training models.



Big Tech Companies Release Earnings Reports

In the fourth quarter of 2024, the largest US tech companies posted mixed financial results, reflecting unique successes and ongoing challenges across the sector. While Meta and Microsoft exceeded expectations, Tesla and Apple faced significant headwinds from shifting consumer demand and macroeconomic pressures.

Meta Platforms posted a 50% rise in net income, with revenue growing 21% to $40.1 billion, driven primarily by a rebound in digital advertising. The company emphasized its continued investment in artificial intelligence (AI) to enhance content recommendations and ad targeting across Facebook and Instagram. Similarly, Microsoft also delivered strong results, reporting $62 billion in revenue, an 18% year-over-year increase, surpassing Wall Street expectations. The company's cloud computing division remained the primary driver of growth, with Azure revenue rising 30%.

Apple reported revenue of $119.6 billion, marking a 2% year-over-year increase. The company's strong iPhone sales helped drive growth, but weaker demand in China led to a 13% decline in Mac revenue. Meanwhile, Apple's services segment, which includes the App Store and iCloud, saw an 11% increase, helping offset some of the declines in hardware sales. Tesla, on the other hand, struggled in the fourth quarter, falling short of earnings expectations. The company reported $1.58 billion in EBIT, significantly below the $2.70 billion consensus estimate. Net margins declined to 6.2%, which is also below the expected 9.9%.

Sources: Reuters, Wall Street Journal

HSBC Retreats From The West to Focus on Asia Aad The Middle East

HSBC is making its biggest investment banking shake-up in decades, pulling back from M&A and equity businesses in Europe and the Americas to sharpen its focus on Asia and the Middle East. Under new CEO Georges Elhedery, the bank aims to streamline operations and increase profitability with a financing-led model centered on regions where it already sees strong growth.

The decision has sparked mixed reactions. Some insiders question the timing, given expectations of a capital markets rebound fueled by interest rate cuts and pro-growth policies in the West. Others argue it's a smart move, cutting loose businesses where HSBC has struggled to compete with U.S. heavyweights.

While the bank will retain its debt capital markets and leveraged finance operations globally, the exit from key advisory roles raises concerns about how it will support these areas without a strong M&A presence. Still, for HSBC, this pivot reflects a clear strategy: focus on markets where it wins, and step back where it doesn't. Despite the bold move, the market's response was muted, with shares dipping just 0.2%.

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