TIM
UNDERWOOD

Newsletter – April 2025

My April 2024 newsletter (attached) was published on 6 May 2024 and had a chart showing how the price of gold, then at $2,326, was ready to break out higher after a long consolidation period. That is exactly what happened and today gold trades around $ 3,300 a rise of $1,000 or plus 40%. This rise in 2024 and into the first part of 2025 is a reflection of weaker currencies with the US dollar, Euros and British pounds all losing value compared to gold. It therefore made sense to have a meaningful allocation to this asset class but the chart makes the case that this is just the begining.

If you look at the April 2024 chart it is interesting to see that the expectation was that after the breakout it would pull back at around $ 3,250 and this is exactly what happened! If this continues to develop as expected in the chart, then we will see an even stronger gold price in the coming years. Nobody knows the future, but it does make sense to hold some gold in a portfolio.

One of the typical economic developments that supports the gold price is falling global interest rates. After the covid lockdowns the resulting supply shock lead to inflation in the main economies and central banks did what they always do in such circumstances and increased interest rates. It was the quickest increase in history but now they are reversing and lowering them. The Swiss central bank leads the way cutting rates all the way down to 0.25%. The ECB followed lower, now down to 2.4% and on 8th May the UK cut rates to 4.25%. The UK decision was odd in that 5 bank members voted for the cut, two more voted for no change and 2 voted for a bigger cut! Even with all the data in front of them central bankers can have three views on the appropriate monetary policy.

Central bank monetary policy it is claimed, is important when managing an economy but what if they are just following the market. The US did not cut interest rates on 7th May and left them at 4.5% but the US bond market has 2 year rates today at 3.9%. Why would a big investors like a pension fund or an insurance company buy a 2 year bond offering a lower rate when the over night rate is higher? Because they believe rates will fall and it is better to lock in the 2 year rate today.

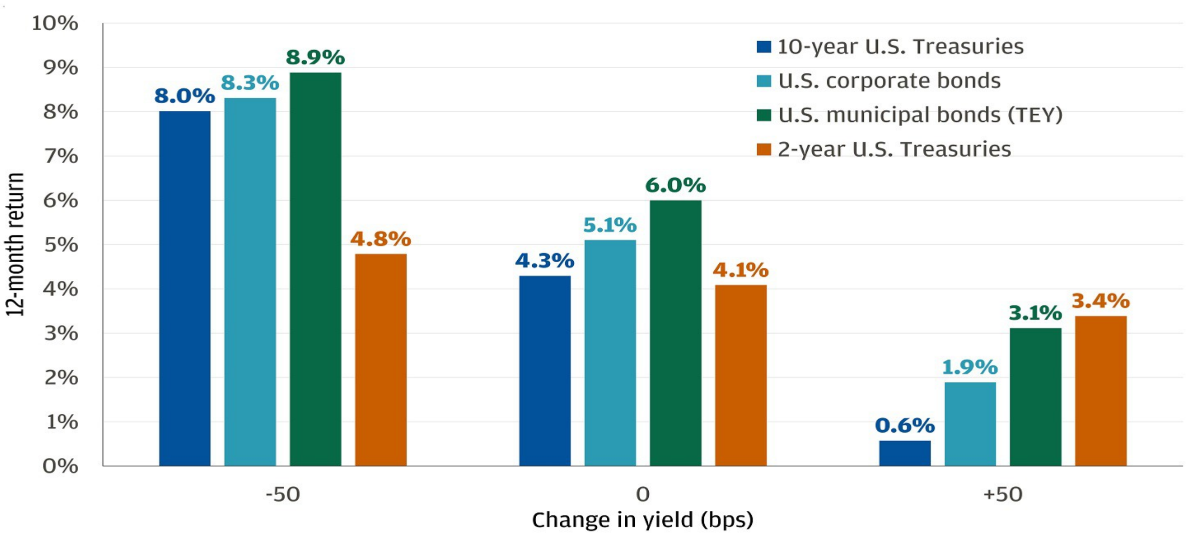
The classic central bank policy response to a recession is to lower interest rates, but some argue that they are always behind events and just follow the market. If this is the case and global recession develops then we can expect even lowers rates as central banks catch up with the market. Europe is already in recession. China has problems (GDP numbers very suspect) so the question is what will happen with the huge USA economy in the year ahead?

New USA tariffs, it is claimed, will put up inflation but what if they do not and turn out to be recessionary. Then interest rates will go lower and the beneficiaries of lower rates are gold and bonds. The chart last year showed the gold situation and below is a chart from a US bank about bonds.

It shows the expectation of bond values if rates go down by 0.5% or stay the same or increase by 0.5%. It was dated the end of February 2025 and as we have seen there is pressure on central banks to lower rates this year. It seems to me therefore that some bonds in a portfolio also make sense at the moment.

There is asymmetry in fixed income returns

Fixed income returns given yield move scenarios



Source: Bloomberg Finance L.P. Data as of February 26, 2025.

Best wishes

Tim Underwood 9 May 2025

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