# Markets under pressure: what's driving the turbulence?

**Recent volatility has unsettled investors, but understanding the forces at play and considering the long-term outlook can help put the bigger picture into perspective.**

## Introduction

Financial markets have experienced notable volatility in recent months, with equity and bond markets reacting to a mix of economic data, policy shifts and geopolitical developments. For investors, these fluctuations can be concerning, particularly when markets move lower in tandem.

However, it's important to remember that volatility is a natural part of investing, and short-term market movements should always be viewed in the context of a longer-term strategy. While recent declines may seem unsettling, they reflect an evolving economic landscape rather than a fundamental breakdown in financial markets.

This update provides a clear explanation of what's happening in global markets, why stock prices have fallen recently, how bond markets have responded and what the outlook is from here. It also underscores the importance of staying invested and maintaining a long-term perspective.

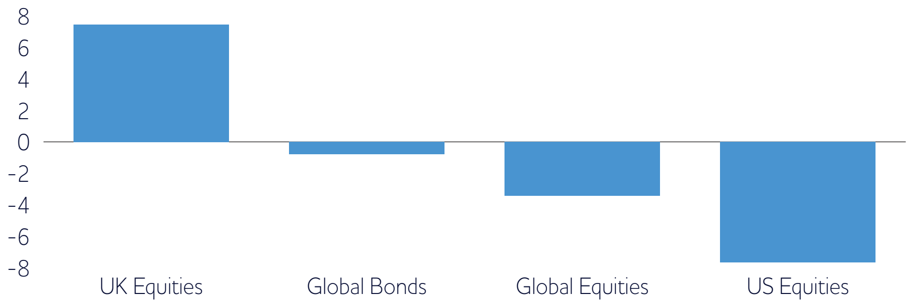
## 1. Recent market declines: what's been happening?

Since the start of the year, global stock markets have faced renewed pressure. The strong performance of US equities, which had led the market for several years, has started to fade. European and other international markets, previously lagging behind, have now caught up, with some even outperforming their US counterparts.

The S&P 500, a key benchmark for the US stock market, has struggled relative to other regions. European equity markets have gained ground, supported by improving economic data and more supportive interest rate policies from central banks.

Investors have also been adjusting their expectations for interest rate cuts, which has influenced equity market performance. Many had anticipated earlier rate cuts from the Federal Reserve, the US central bank, but with inflation remaining higher than expected, the US central bank has signalled a more cautious approach. This has dampened investor sentiment and contributed to the pullback in stock prices.

### Figure 1: Stock market returns since the start of 2025 (in sterling)




Source: FE Analytics as at 18 March 2025. Indices are FTSE 100 Index, ICE BofA Global Broad Market Index, MSCI ACWI Index, S&P 500 Index. All returns are in GBP.

## 2. Why have stock markets fallen recently?

Several factors have contributed to the recent downturn in global equity markets. These include economic uncertainty, changes in interest rate policy expectations and renewed trade tensions:

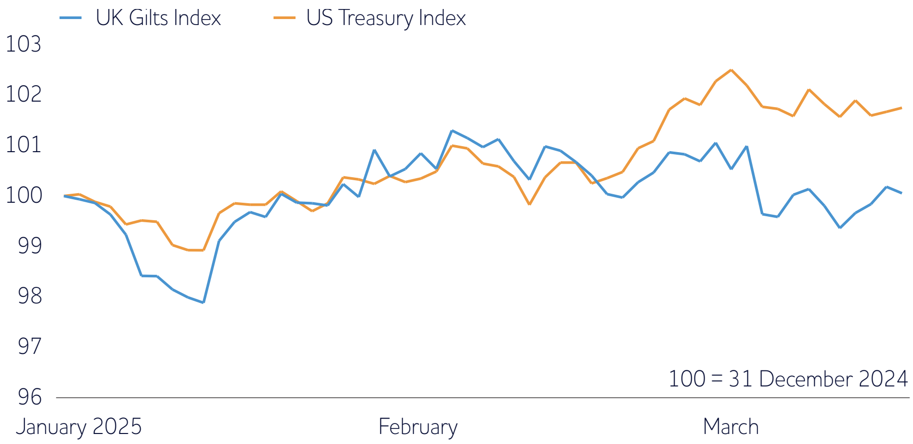
- **Policy uncertainty in the US.** Political and fiscal policy decisions in the US have been a key source of market uncertainty. Recent government debates on spending and taxation have weighed on investor confidence, making it harder to predict the future direction of economic growth.
- **Trade tensions and tariffs.** Trade policy has also played a significant role in shaping market sentiment. The US administration has announced or implemented a series of new tariffs on goods imported from the EU, Canada, Mexico, and China. These measures have sparked fears of rising costs for businesses and consumers, potentially leading to higher inflation. China has responded by imposing tariffs on $14 billion worth of US exports, targeting industries such as energy and agriculture. These developments have increased concerns about a prolonged trade dispute, which could impact global economic growth.
- **Inflation concerns and interest rates.** Inflation remains a persistent issue in major economies. In the US, inflation rose to 3% in January, up from 2.9% the previous month, reducing expectations for early interest rate cuts. Higher-than-expected inflation has led central banks to adopt a more cautious approach. Investors who had been hoping for more rapid cuts in interest rates have had to reassess their outlook, which has contributed to the volatility in financial markets.
- **Global economic divergence.** While US economic growth appears to be slowing, other regions – particularly Europe – have been more resilient. European markets have performed well in recent months, buoyed by strong corporate earnings and interest rate cuts from the European Central Bank. In contrast, US equities have struggled, as businesses and consumers adjust to higher borrowing costs and ongoing trade uncertainties.

## 3. What's happened in the bond markets?

Bond markets have played an important role in stabilising investor portfolios amid equity market volatility:

- **UK bond yields spike before easing.** In the UK, government bond yields rose sharply before falling back down. As bond yields fall, bond prices rise. This reflects changing investor expectations around inflation and interest rates. While higher yields can lead to short-term declines in bond prices, they also present an opportunity for investors to earn a more attractive income from fixed income securities.
- **Bonds as diversifiers.** Global bond markets have provided some relief for multi-asset investors, helping to offset losses in equity portfolios. This highlights the importance of diversification – when stock markets struggle, bonds can help cushion the impact and reduce overall portfolio risk. This is particularly true in the US, with US government bonds, known as Treasuries, delivering positive returns so far this year, while US equity markets have fallen.

Figure 2: US Treasuries have outperformed UK gilts since the start of 2025




Source: Bloomberg as at 19 March 2025.

- **Interest rate expectations and bond performance.** Looking ahead, bond markets are likely to benefit if central banks continue to reduce interest rates later in the year. Falling rates typically lead to higher bond prices, which could improve returns for investors in fixed income assets. In the meantime, we are able to benefit from the strong yields (or income paid from the interest) that bonds are offering.

## 4. What is the outlook from here?

- **Equities remain sensitive to macroeconomic factors.** Given ongoing trade tensions, inflation concerns and shifting interest rate expectations, stock markets may remain volatile in the short term.
- **Bonds could see improving returns.** Now interest rates have potentially reached their peak, the potential outlook continues to be more attractive. Investors in fixed income could benefit from both higher yields and potential price appreciation if central banks continue reducing interest rates.
- **Europe may continue to outperform.** European markets have demonstrated resilience, supported by strong earnings and interest rate cuts from the European Central Bank. This trend could continue if economic conditions remain favourable.
- **The Federal Reserve has downgraded its economic outlook.** In its latest statement, the Fed signalled a more cautious view on US economic growth, citing persistent inflation pressures and signs of slowing consumer demand. This has reinforced expectations that interest rate cuts may come later than previously anticipated, adding to market uncertainty.
- **The risk of recession remains.** While most economists expect a soft landing, the Fed's more downbeat outlook has increased concerns about a potential slowdown. Active management of portfolios becomes more important in these more uncertain times.

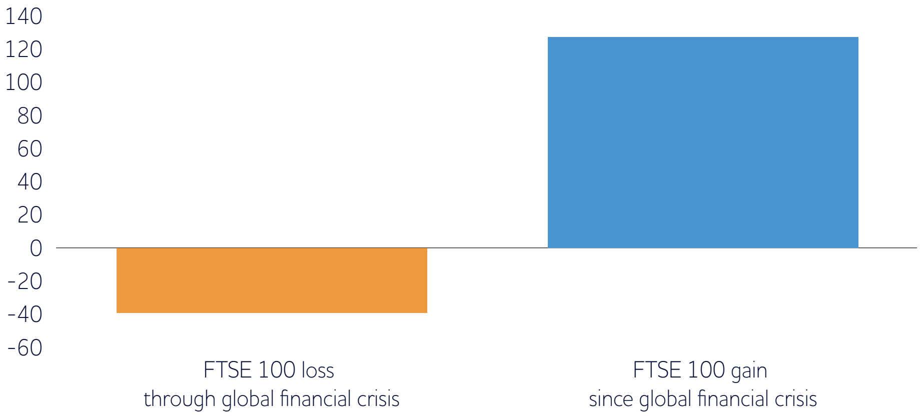
## 5. Why is it important to stay invested?

During periods of volatility, it can be tempting to move to cash or reduce exposure to risk assets. However, history shows that remaining invested tends to yield better long-term outcomes.

- **The risk of missing market recoveries.** One of the biggest dangers of trying to time the market is missing the recovery. Many of the strongest stock market gains occur in short bursts, often following a downturn. Investors who exit during periods of uncertainty may miss out on these rebounds. For example, during the 2008 financial crisis, the S&P 500 experienced a sharp decline, but investors who stayed invested saw a 109% return over the following five years.
- **Market cycles are inevitable.** Market fluctuations are a normal part of investing. Over the long term, stock markets have tended to reward investors who remain patient and focused on their financial goals.

Similar to the example mentioned above, the FTSE 100 faced a sharp decline through the 2008 financial crisis, but staying invested reaped rewards for investors.

Figure 3: Despite setbacks, financial markets tend to rise over time (%)



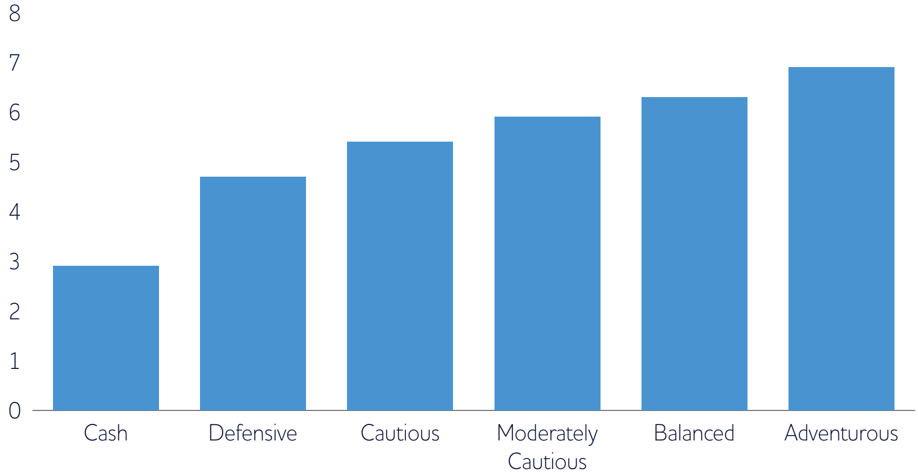

Source: Bloomberg as at 19 March 2025

## 6. What is the long-term outlook for portfolios?

While short-term market movements can be unsettling, the long-term outlook is still positive.

- Expected returns for diversified portfolios remain attractive. Over the next 10 to 15 years, cautious through to adventurous portfolios are projected to deliver steady returns. These expected returns have accounted for the fact that over a 10- to 15-year period, markets will go through shorter-term bursts of volatility like we are seeing in current market conditions.
- Investors should stay focused on their financial objectives. Short-term volatility should not distract from long-term investment plans.

### Figure 4: Expected long-term annualised returns by risk profile (%)




Source: Omnis Investments as at 31 January 2025. Expected returns are annualised and derived from J.P. Morgan Long Term Capital Market Assumptions.

The value of your investment and any income from it can go down as well as up and you may get back less than you invested.

## Find out more

If you have concerns about your portfolio, consider speaking to your financial adviser. They can help ensure your investment strategy remains aligned with your long-term goals. Your financial adviser will also be able to help you with any other issues, such as meeting short-term cash needs while making sure your long-term investment plan remains on track.



Approved by Omnis Investments on 20 March 2025