VIG HOUSE VIEW

VIG ASSET MANAGEMENT HUNGARY

What happened in the last month?

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- Investment Clock
- Tactical asset allocation
- Focus funds
- ESG theme of the month

DECEMBER 2024

WHAT HAPPENED **IN THE LAST MONTH?**

US TARIFF WAR IN FOCUS: RISKS AND SIDE EFFECTS

The world

Investors and economists around the world are speculating on the measures Donald Trump will take once he's back in power. Indeed, the protectionist plans that the US president elected in November has already hinted at could seriously disrupt entire national economies and the capital markets. The biggest impact of these plans could come from "safeguard tariffs": a 10-20% tax on all imported goods and a whopping 60% levy on Chinese imports (though more optimistic pundits suggest somewhere just north of 40% is more likely), which Trump will impose in January to protect domestic industry.

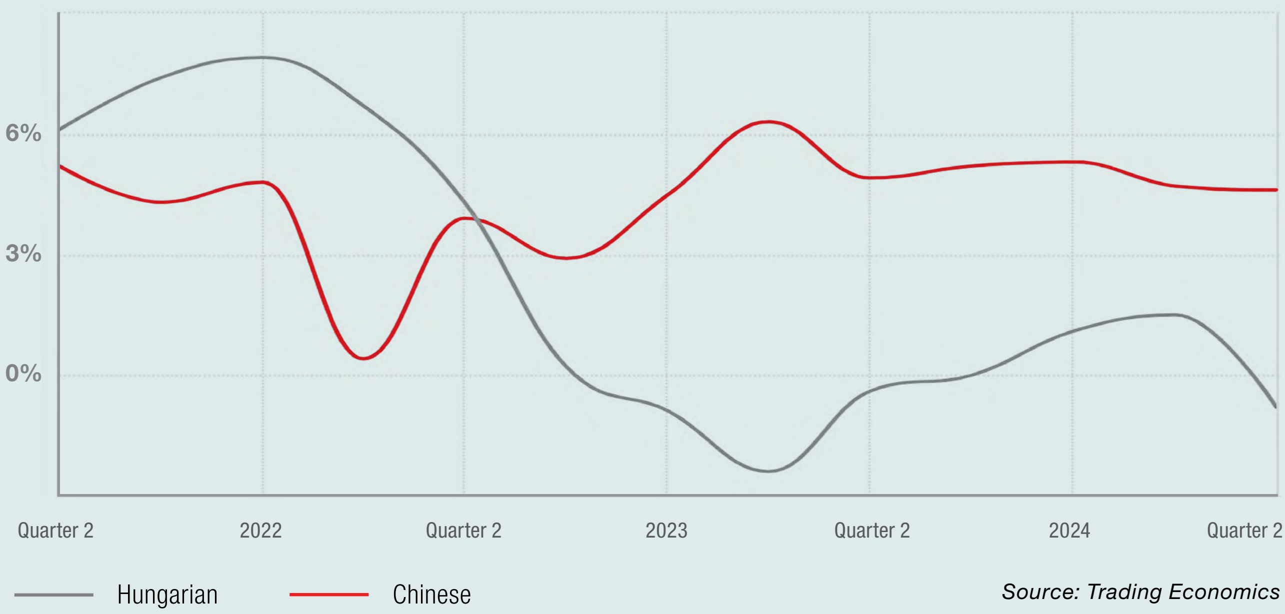
As the US, the world's number one economy, is an important market for almost every major country from Europe to Asia, the proposed measures could mean a huge blow to them: Estimates suggest, for example, that China's GDP growth in 2025 could be set back by a full percentage point if the measures are approved. Since Europe's growth is more fragile than that of the US, a trade war of this sort could further damage the prospects of the European continent and by extension, those of Hungary, which supplies it.

In the short term, however, these expectations could lead to a temporary economic spike, as foreign companies supplying the US market ramp up their production in order to ship as many goods as possible to the New World before the tariff hikes take effect. China's steel exports, for example, could rise to an eight-year high (109 million tonnes) before falling back to 96 million tonnes in 2025 due to the massive tariffs.

Hungary

As a small, open economy, these developments could affect Hungary too (the United States is the largest non-EU investor in Hungary and its most important export partner outside Europe) – and a positive stimulus, however modest, could not come at a better time. The 0.7% contraction in domestic GDP in the third quarter due to weak car and battery production as well as the summer drought point to a technical recession. The suffering of the Hungarian economy is reflected in the fact that it has only grown in three of the last nine quarters.

Chinese and Hungarian GDP growth



Source: Trading Economics

WHAT HAPPENED **IN THE LAST MONTH?**

EQUITY MARKET NEWS

It's good times for stock markets, as reflected in equity prices: the S&P 500 stock index, which shows the average change in the price of shares on the New York trading floor, has risen to a new historic high of over 6000 points – bringing this year's dollar-based return to over 25 (!) percent. The rise is not surprising: the macroeconomic environment is supportive (a soft landing without a recession, coupled with interest rate cuts, which is still the most likely scenario for equities), and following the US presidential election there could be a significant flow of capital from large-cap equities to smaller ones, as well as from the EU to the US. The earnings outlook for US companies is also promising, with fourth-quarter 2024 revenue growth at a three-year high. This good run could continue in 2025, with double-digit earnings growth currently expected for each quarter (12.7%, 12.1%, 15.3% and 17.0%), and with the best performing sectors being IT, communication services, consumer durables and real estate. However, the fact that US stock markets are currently expensive gives reason for caution: the average P/E ratio of US stocks, at above 20, exceeds the average of several decades. Europe, on the other hand, is underperforming, as we've already pointed out, and the "war discount" has increased further in our particular neck of the woods. The latter could also represent a good buy point for savvy investors, with the Central and Eastern European region's stock markets looking very cheap in light of their growth potential, and with the resolution of the Russia-Ukraine conflict prices could rise sharply.

WHAT HAPPENED **IN THE LAST MONTH?**

BOND MARKET NEWS

Donald Trump's election victory and the Republican majorities in the Senate and the House of Representatives are expected to allow many of the new president's election promises to be kept. The import tariffs and the halting (and possible reversal) of immigration could push up previously planned inflation by an estimated 0.5-1 percentage point, and this may be further boosted by a pick-up in economic activity: businesses have been holding back investment all year due to election uncertainty, but the "Made in USA" trade policy, tax cuts and a general push for business-friendly regulation may reignite investment and hiring.

These expectations are keeping dollar interest rates high (the 10-year US Treasury bond yield is currently well above 4%), which could mean a good entry point for investors. As Europe is facing significant economic problems (low GDP growth, large budget deficits), this could also lead to a short-term appreciation of US bonds, as seen in the French government crisis in early December and the subsequent dollar bond rally. However, moderate economic growth in Europe could be supportive for continental government bonds: by 2025, businesses can expect lower interest rates than today.

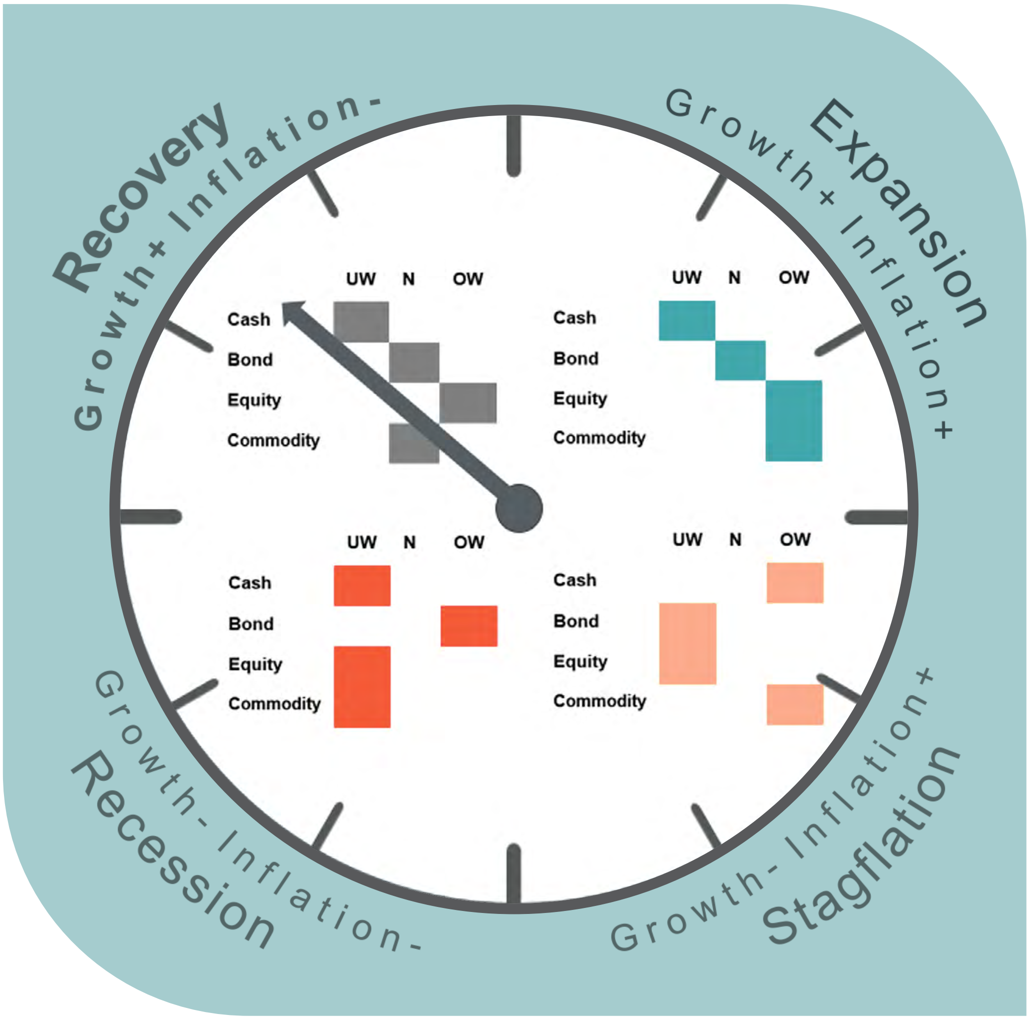
ALTERNATIVE INVESTMENTS NEWS

Although there were signs of hope in September when the Chinese government announced a stimulus programme to boost liquidity, the impact was short-lived and thus the bounce in commodity market prices proved to be only temporary. The reasons for this include the strengthening dollar, which traditionally results in falling world market prices (as a dollar-denominated commodity becomes relatively expensive in other currencies), and, of course, the planned "trade war" of US President-elect Donald Trump. The global price of gold also flatlined in November, though its price has still risen by nearly 30% since the start of the year and, as a safe haven asset, it can prove a useful longer-term component of a portfolio amid geopolitical and economic-policy concerns.

WHAT CAN WE EXPECT **IN THE COMING PERIOD?**

INVESTMENT CLOCK DECEMBER: RECOVERY

The world economy remains in a recovery phase overall, though the trajectories of the individual regions are different. In the United States, the tightness of the jobs market, disrupted by hurricanes, Boeing strikes and layoffs at key automakers, is decreasing. Previous forecasts published in the autumn had hugely overestimated the recent upswing in the US economy, a potentially worrying sign in itself – and the slowdown in jobs growth is shaking confidence in the economy. Deflation is also slowing, mainly due to rising house prices: although interest rate hikes have made credit more expensive (the annual interest rate on a 30-year mortgage is currently 6.5%), the median price of second-hand homes has risen by 4% to $407,200. Europe's economy, on the other hand, is clearly struggling: foreign demand is weak, fewer electric cars are being sold in Germany due to declining government subsidies, and Volkswagen is struggling to survive with a €4 billion cost-cutting programme that will require the closure of several of its factories. And Moody's has downgraded France's debt rating outlook to negative because of its huge budget deficit of 6% of GDP.



OW: Assets expected to perform well in the given period.

N: Assets expected to perfom less well in the given period.

UW: Assets expected to perform poorly in the given period.

Source: VIG Asset Management

WHAT CAN WE EXPECT **IN THE COMING PERIOD?**

TACTICAL ASSET ALLOCATION

- The outcome of the US presidential election could be positive for US equities, as the possible imposition of tariffs will give companies producing for the domestic market an edge over foreign competitors.
- The recovery phase, as indicated by the Investment Clock, and the rising expectations for a no-landing scenario could have a positive impact on risk assets at the end of the year. This could provide an opportunity to take advantage of the further upside potential of US equities, as well as the very attractive valuations of Central and Eastern European equities.
- Despite the improving economic outlook, we believe that developed market bond yields have reached a level that could technically provide a favourable entry point in the short term, while emerging market bond prices are on the high side right now.

MONTHLY ASSET ALLOCATION (DECEMBER 2024)

Asset class	H UW	UW	S UW	N	S OW	OW	H OW	Change
Cash (Money market)			■					↓
Fixed income				■	■			↓
Core market fixed income					■			
EM local currency bonds			■					↓
EM hard currency bonds			■					↓
CEE government bonds				■				
Commodities				■				↑
Gold				■				↓
Equities					■			↑
DM Equities				■				↑
US Equities					■			↑
EU Equities				■				
EM ex China Equities				■				
CEE Equities					■			↑

Changes – change compare to the the previous month

The table was prepared based on our investment clock and quadrant model.

Weights:

The weights indicate the evaluation of the respective country, region, and asset class, providing a basis for portfolio managers in structuring portfolios and establishing positions, thus helping to capitalize on market opportunities.

- Strongly underweight
- Underweight
- Slightly underweight
- Neutral
- Slightly overweight
- Overweight
- Strongly overweight

WHAT CAN WE EXPECT **IN THE COMING PERIOD?**

FUND OF THE MONTH

VIG ACTIVE BETA FLEXIBLE ALLOCATION INVESTMENT FUND

The VIG Active Beta Flexible Allocation Investment Fund offers an active portfolio management approach that is well suited to the current market environment and aims to achieve capital growth through investments in US and European companies. Strong economic activity and positive corporate results should continue to support US equities. The positive effects of the presidential election could benefit companies producing for the domestic market. The broader-based rise in the US stock market (S&P 500) shows that growth is not just driven by the results of a few large companies. Technical indicators also point to a continued positive outlook, which could create a favourable investment environment. Given the attractive valuations and growth opportunities there, the Western European and Central and Eastern European markets are also a key focus of the Fund's strategy. The Fund's active portfolio management approach allows it to react dynamically to market changes. This is particularly important in the current fast-changing economic environment, where a flexible strategy is key to maximising returns. The VIG Active Beta Flexible Allocation Investment Fund may be the ideal choice for those who want to take advantage of the current favourable market conditions and grow their capital over the long term.

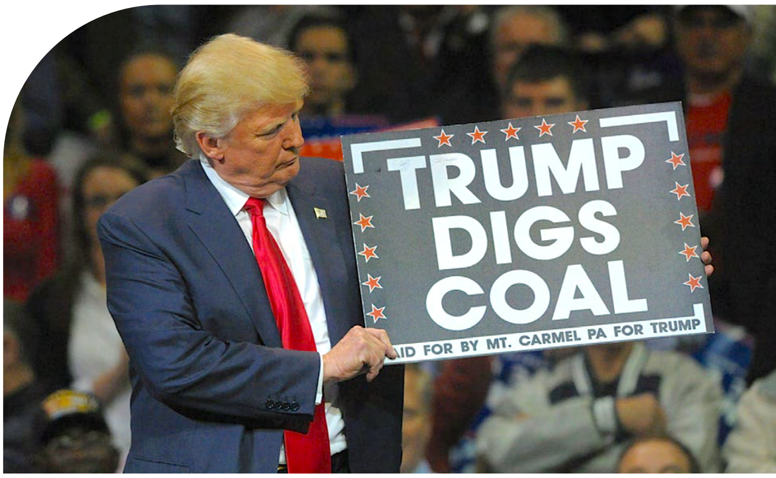
ESG THEME OF THE MONTH

TRUMP'S SECOND ACT: a green light to reverse course?

The recent US presidential election is expected to have a major impact on ESG (environmental, social and governance) issues. With the return of Donald Trump, experts have expressed concerns about the future of US action on climate change and ESG. Trump's political views and the measures he took during his previous presidency suggest that the impact on the green economy could be negatively skewed during a second presidential term.

During his first presidency, Trump abolished many environmental regulations and orchestrated America's withdrawal from the Paris Climate Accord. Officially, there is a one-year period between the announcement of withdrawal and actual withdrawal, and so the withdrawal request submitted in 2019 entered into effect on the very day that Democratic President Joe Biden won the election. Biden signed the papers on rejoining the accord on his first day in office, meaning that Trump's measures had kept the US out of the Paris Agreement for less than four months. But Trump pledged to withdraw the US from the Paris Climate Accord for a second time during his 2024 presidential campaign. From an ESG perspective, this means there'll be less pressure on companies to adopt more sustainable practices, which in the long run could be detrimental to the development of the green economy.

The second Trump administration is also expected to challenge the climate rules introduced by the Biden government. The US Securities and Exchange Commission (SEC) climate risk disclosure rule could be one of many such measures that Trump will seek to undermine. This rule has been suspended since early April, almost a month after its adoption, as Republican-led states have questioned the agency's right to promulgate the rule. The final rule would aim to promote transparency and corporate responsibility in tackling climate change. If Trump reverses its adoption, it could reduce corporate responsibility for environmental impacts. This would have a negative effect on ESG efforts and on the publication of standardised, comparable, climate-related disclosures that investors are increasingly calling for.



https://www.verdict.co.uk/trump-threatens-esg-progress/

Trump's re-election could have an impact not only on the United States, but also globally, as the US commitment to fighting climate change could influence other countries' policies and co-operation. If the Trump administration reverses course on green initiatives, it could encourage other countries to take similar steps. Some fund managers, investors and clean energy executives are somewhat more positive in their view of the matter, saying that Trump's proposed policy measures could be held in check by political considerations and market demand for renewables. Alex Monk, a portfolio manager for Global Resource Equities at Schroders, wrote: "... policy is not the only driver of the energy transition, and the US is not the only market for companies across the space." He also pointed out that "while the shifting US policy landscape is undoubtedly unhelpful, it should not distract from the strength of other forces encouraging investment in the space."

Overall, Donald Trump's re-election could lead to a reversal of environmental regulations and a reduction in corporate responsibility, which in the long term could have a negative impact on ESG efforts in the US at the least, but possibly also in other countries. However, we believe that the European Union and other countries may react differently. It's conceivable that the possible US backtracking on ESG regulations could trigger a response in other countries to increase the number and improve the quality of ESG regulations. For example, if the United States cuts funding for renewables, Europe could regain its competitive advantage in sectors such as wind and solar.

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