A forward view of the global economy and financial markets

March 2025

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Housebuilding

"There are no excuses not to build 1.5 million new homes".
Deputy Prime Minister Angela Rayner, March 2025

Source: Wikipedia

Many people would say that it is the triumph of hope over expectation to think that 1.5 million new homes will be built in England by the end of 2029. History, as well as the building industry, tell us that it is very unlikely that we will get anywhere near achieving Angela Rayner's target.

Between 1945 and 1970, a housebuilding boom occurred. During this period, private housebuilding fell by more than public housebuilding increased, a classic case of the public sector squeezing out the private sector. Since the peak in 1970 a steady decline has been underway. This fall paused slightly in the 1980s before falling back to the lowest peacetime level since the 1920s between 2010-15.

The Government's aim is to now build 300,000 new homes a year for 5 years. The last time that figure was achieved was in 1969-70 under Labour's Harold Wilson and one would have to say that it was a case of never mind the quality and certainly don't feel the width. Some of the ugliest and badly made houses were built in this period but this is not surprising if you are simply chasing numbers rather than worrying about the quality. Then by 1978-79 a mere 93,000 new homes were built.

Recent numbers have been better but are now declining again. New home completions were 253,000 in 2022, 231,000 in 2023 and 217,911 in 2024. The problems for the housebuilding industry are well known. Planning permission and available land for new housing developments in areas of England where the demand for new homes is most pressing has been at the heart of the problem. There is also the question of the building industry's capacity to actually deliver 300,000 new homes a year.

The cost of building materials has risen by 35% since 2021, labour costs have risen significantly and are set to rise further after 6th April this year, thanks to the Chancellor's 2024 Autumn Statement. It is estimated that the UK construction sector will be facing a labour deficit in skilled workers such as bricklayers, carpenters and plumbers of 225,000 by 2027 if Angela Rayner's targets are to be met. It is hard to imagine that nearly a quarter of a million new skilled workers are going to be available by 2027. As we are no longer part of the EU we cannot look to Europe to plug the gaps in our labour market and we are not training enough apprentices to make up the shortfall.

The average number of new homes that were required per year from 2024 is actually 370,00 and no matter how swiftly we grant planning permissions to housebuilders, we know they do not have the physical ability to make 370,000 new homes a year for five years. There is also the question of what type of housing are we going to build. Will it all be affordable housing? If that is to be the case we will be flooding one end of the housing market with cheap houses which will probably drive house prices down. This will, in turn, hurt the profits of the housebuilding companies therefore disincentivising them.

There is general agreement that we need to increase the number of new houses built in the areas of England where they are most needed. We need to improve the quality of construction and we need to train many more people in the skills that are essential to the industry. Setting unrealistic targets is never a good idea, it will just result in a glut of wrong type of housing, in completely the wrong areas, built to a very poor standard of workmanship, just so that a political party can say they have delivered on a manifesto pledge.

Richard Harper
Head of Asset Allocation
GHC Capital Markets Limited

Asset Allocation

In which **Tim Harris**, the Chair of our Asset Allocation Committee, describes the factors influencing our latest Asset Allocation decisions

Are We Getting Used to the Noise? – Sort of

Markets adjust to uncertainty over time. When President Trump took office in January, expectations ran high that his second stint at the White House would be characteristically different. Indeed, as the president embarked on aggressive policy posturing, even his supporters were often caught off guard by the unpredictability of his actions — whether it was about dismantling previous policies or challenging constitutional norms. Yet, markets learn to adapt. As Trump announces yet more tariffs, the market reaction will likely be more muted than in the past, as investors have grown accustomed to his unpredictable stance on policymaking. This resilience helps explain why the volatility in the broader S&P 500 has eased recently.

Focus on What's Important

With so much confusion in the markets it's easy to lose way even as a myriad of topics seemingly drive investor sentiments. From tariffs, immigration, and DoJ speeches to the situation in Ukraine, Yemen, and Gaza, none of us can predict the outcomes for all of these events with precision. It is therefore better to focus on an outcome that has a more direct bearing on the markets — and, in this case, we point to US growth and inflation.

Growth: According to Bloomberg, the consensus expectation is for 2.2% growth in 2025, although quite a few of the economists polled have trimmed their forecasts to numbers below 2%. Recent examples include:

- Goldman Sachs reduced its 2025 GDP growth forecast to 1.7% from 2.4%, citing the adverse effects of increased tariffs on imports from Canada, Mexico, and China.
- Vanguard projects a 1.4% GDP growth for 2025, acknowledging downside risks due to tightening financial conditions and emerging weaknesses in the labour market.
- The Congressional Budget Office forecasts a decrease in economic growth to 1.9% in 2025 from an estimated 2.3% in 2024, with growth retreating further to 1.8% in 2026.
- Deloitte expects real GDP to grow 1% in 2025, supported by resilient consumer spending, partly because of anticipated increases in the minimum wage.

Inflation: A Temporary Calm or a Looming Storm?

So far, inflation has remained relatively well-behaved — but risks to the upside persist. The latest data suggest inflation trended slightly lower in February. While the decline isn't dramatic, it has provided some comfort to the markets. Notably, bond market volatility remains below long-term averages. However, market expectations for future inflation tell a different story. Since September, forward inflation pricing has surged, now sitting about a percentage point above the Fed's comfort zone. The two-year breakeven inflation rate in the inflation-linked bond market has risen above 3%, signaling growing concerns.

Surveys of industrial and consumer sentiments have shown a spike in expected inflation. The University of Michigan's consumer confidence data released last week showed households anticipating a surge in inflation over the next 12 months. Just a few months back, households expected inflation to be around 2.6% in 2025. Given the current policy uncertainty and looming tariffs, that expectation has now soared to 4.9%. Energy prices, which have been flat over the past few months, aren't the culprit. Consumers see trouble from the unknown factor of tariffs.

The logical Outperformance of EAFE equities versus the US

For years, US economic growth has been propped up by ever-increasing debt. Are they living beyond their means? The numbers tell a story: Germany's debt-to-GDP ratio stands at 63%, while the US's has reached an unsustainable 120%. Given the current uncertainty, there is market logic behind the recent outperformance of global equities vis-à-vis the US market. The valuation premium of US equities over the rest of the world (Europe, Australasia, and the Far East, or EAFE) remains near historic highs, yet the perception of US market exceptionalism may be overstated.

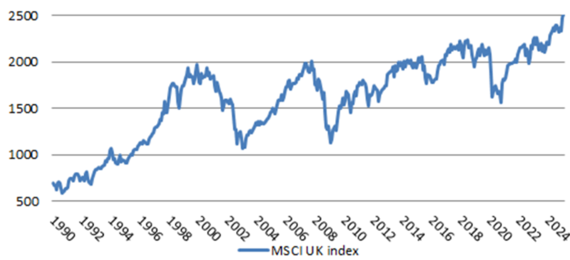
We expect recent outperformance of European and Asian equity markets relative to the US to continue

A period of outperformance is only just starting to reverse years of underperformance. A key driver of this outperformance is the improving relative fundamentals of markets outside of the US. Take Europe, for instance, where Germany, among other nations in the continent, is significantly increasing its defence budget, signaling greater fiscal flexibility and a willingness to recalibrate but not exaggerate debt-to-GDP ratios.

We have reduced the risk profile across our managed portfolios since the New Year

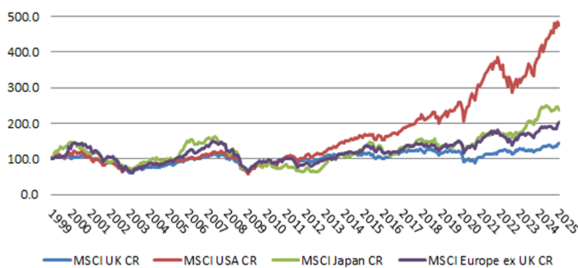
We have increased our weightings to European equities. With inflation risks ascendant, we retain a shorter duration in the fixed income elements of portfolios — we may see yet higher yields in bond markets as summer unfolds. After the strong returns of the last year, this may be a time for consolidation in global markets.

Markets at a Glance



Source: Lipper for Investment Management

Since the October Budget we have seen: i) employment surveys deteriorate sharply as companies – looking to compensate for the tax rises they face – hire fewer workers, with the British Retail Consortium cautioning that up to 160,000 part-time retail jobs could be lost in the next three years, ii) companies raising prices given higher staff costs and iii) rising prices, along with higher energy costs and VAT on school fees, has pushed up headline inflation. Given both greater domestic exposure and a greater share of debt with floating interest rates, higher inflation tends to hit UK small cap performance versus large cap.

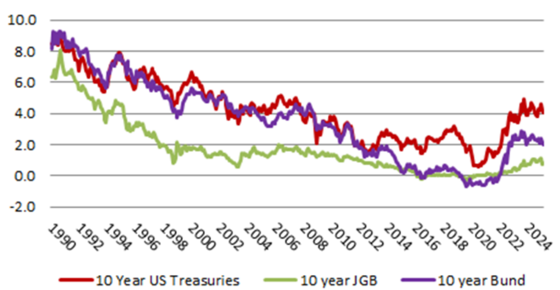


Source: Lipper for Investment Management

Confidence in US 'exceptionalism' was running high at the end of the last year. Since then, relative returns have inflected, the US has corrected, and diversification is paying off. There are three drivers. First, US growth is moderating from a high level and improvement elsewhere, particularly, in Europe. Second, tariff fears and uncertainty are starting to weigh more on US confidence than elsewhere, driving higher US risk premia. Third, the high stock and sector concentration in the US is acting as a headwind to index returns as the largest companies are underperforming. We recommend broad diversification by geography, sector and factor.

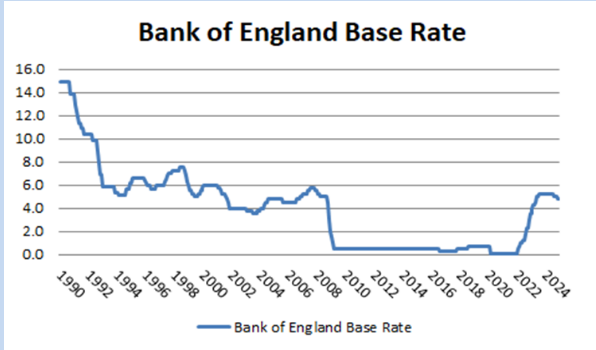
Source: Lipper for Investment Management

The recent rise in UK yields has accelerated the move that started back in September. Gilts initially sold off into the October budget, then continued following the US election. Much of this sell-off represented an increase in term premium. Despite this, ongoing progress on underlying inflation and gradual rate cuts from the BoE may serve to anchor the Gilt curve, and ease digestion of elevated Gilt supply, especially in the context of a reduction in the pace of BoE Gilt sales. This should ultimately see a lower fiscal risk premium across the Gilt curve. We expect 10 year Gilt yields at 4.00% at end-2025.



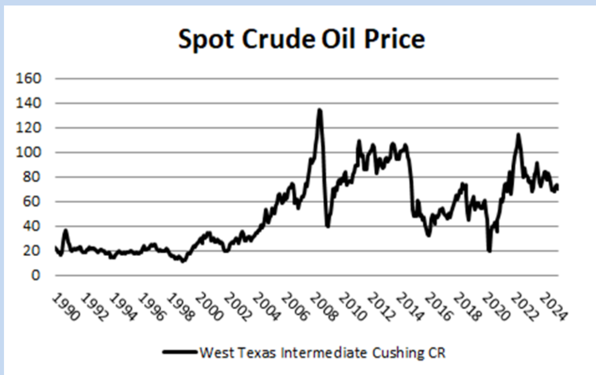
Source: Infront

The sharp rally in US yield levels from mid-February into early March has given way to a period of consolidation. Risk assets have suggested a further weakening in the growth outlook, but the backdrop for yields has been more complicated, as growth worries have coincided with upside risks to inflation and a regime shift in European yields. It is not to say that evidence of downside fears is entirely missing within the rates market, but the impact has been a relative one, visible in the outperformance of the mid end relative to the long end of the curve, as opposed to the outright level of yields.



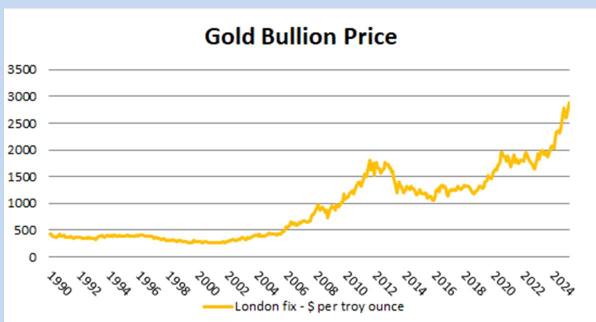
Source: Lipper for Investment Management

The gilt market sell-off raises the stakes for upcoming data – not just on the UK economy, but also financial market variables such as base rates and sterling. Given the likelihood that inflation will not trend down soon, following higher employment market costs, business rates and tariffs, we expect just two base rate cuts in the current year. The upcoming data path will determine Bank of England policy.



Source: Lipper for Investment Management

Brent oil prices have fallen from above $80/bbl in mid-January to $70/bbl despite relatively stable and low inventories. The sell-off mostly reflects a shift in market focus from downside risk to Russia and Iran supply to softer US GDP growth. We now expect oil demand to grow by 0.9mb/d in 2025 (vs. 1.1mb/d prior), incorporating slower US GDP growth on higher tariffs. We also expect somewhat higher OPEC+ supply. We forecast Brent to range $65-80 this year and a 2026 average forecast to $68 for Brent (WTI to $64).



Source: Lipper for Investment Management

Structurally higher central bank demand may add further to the gold price by year-end, which combined with a gradual boost to ETF holdings as the funds rate declines, should outweigh any drag from normalizing positioning, assuming uncertainty diminishes. However, if policy uncertainty - including tariff fears - stays high, higher speculative positioning for longer could push gold prices as high as $3,300/troy oz by year-end. Central bank and other institutional gold demand on the London OTC market was strong at 108 tonnes in December (vs. pre-2022 average of 17 tonnes). China was again the largest buyer, adding 45 tonnes.

Note that where an MSCI Index has been used for illustration. This has been sourced with permission from MSCI Inc.

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