Investment Insights
Lessons from 2024

Morningstar Wealth
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For Financial Professionals Only

Key Takeaways

- A good year for investors
- AI dominance but contrarian plays paid off
- Active asset allocation remains key

Lessons from 2024

2024 turned out to be a much better year for investors than many expected. Fears of recession and resurgent inflation proved ill founded. Elections did not result in large overall market moves and played second fiddle to more fundamental factors. Even escalating conflict in the Middle East failed to trigger a sustained breakout in commodity prices.

Instead, interest rates were reduced and multi asset portfolios outperformed cash and inflation. Being fully invested paid off. It helped to be heavily exposed to the "Magnificent 7" stocks, especially Nvidia, as the spend on Artificial Intelligence capabilities reached new highs.

That AI dominance of markets is an important factor for investors to consider, because it has led to record levels of stock concentration in the US. A handful of companies now play an outsized role: the 6 most valuable companies represent 25% of the US stockmarket index. The US in turn dominates global equity indices, representing 71% of developed world and 63% of developed and emerging combined. Higher concentration has been driven by surging profitability, supercharged by share prices rising faster than earnings. The result is a highly valued US sharemarket.

We see this as an emerging risk rather than something today that justifies moving away from normal levels of risk taking. Our research on overall investment conditions is not flagging an extreme and we can still identify enough opportunities within the US market and elsewhere to be able to generate attractive risk adjusted returns.

Previous instances of highly valued "market darlings" that dominated stock market indices, foretell the need to actively manage asset allocation and to search out opportunities far and wide. Diversifying beyond headline AI themed US companies is now especially important for investors facing a transition to retirement or drawing down on their capital. This challenge is one of the key topics in our 2025 outlook: "Our best investing ideas when the US looks expensive".

Some of these markets also feature in the lesser-known success stories of 2024; US financials (+37%), US utilities (+33%), China (+19%), US small companies (+19%) and Germany (+15%). We still see upside in China and US small caps, given current share prices and greater support from their respective government policies, even with the prospect of increased tariffs. All have been oversized positions in Morningstar multi asset managed portfolios and funds in 2024, reflecting the breadth of our research coverage and the opportunity to profit from excessive pessimism.

The more notable laggard has been the UK stockmarket. Its 11% return while high by historical standards and compared to inflation, paled in comparison to those boosted by AI spending. It remains in our view one of the better valued developed markets and has improved demand/supply balance dynamics with more share buybacks and takeover activity and less structural selling pressure from UK pension funds.

As for bonds, 2024 was a mediocre year with investors having to reign in their expectations for interest rate cuts and concerns that a Trump presidency might add to inflationary pressures and fiscal deficits. Riskier corporate bonds trounced safer government bonds, bringing down yield spreads to the low end of their historic range. We prefer emerging market bonds, as they continue to offer better value even after performing well. Developed government bonds reminded us of their defensive qualities during the mid-year mini-panic, and remain fairly priced with scope to provide diversification and outperform cash. Overall, our key takeaways from 2024 are to be thankful for such returns from equities, expect more normal returns in 2025 and to use active asset allocation to manage the extra risks that come with a highly concentrated and highly priced US stock market.

All sources referenced from Morningstar Direct as at 11/12/2024 unless stated otherwise.

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