

GLOBAL OUTLOOK

March 2025

INTRODUCTION

This document shows the charts that we think are particularly useful to help us determine where we are in the economic cycle and what the outlook is for markets.

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SUMMARY OF OUR VIEWS

MACROECONOMIC BACKGROUND

The mood music has changed in the last month. Since its peak on February 19th the US benchmark S&P500 Index is down 10% and the NASDAQ Composite is down over 14%. The Magnificent 7 index is down 16% as of the 13 March close.

Factors contributing to this include concerns that the economy is slowing and that a recession is possible. The GDPNow forecast for growth calculated by the Atlanta Fed from all the high frequency economic datapoints released is forecasting -2.4% for first quarter GDP. Several large retailers have talked about weaker consumer spending across the income scale. For two weeks from February 26th the US yield curve was inverted from 10 years to 3 months, a classic recession warning indicator.

Bond yields have responded to the changed tone with the 10-year Treasury yield falling by 0.5% from its January peak of 4.80%. Real yields have also fallen. The 10-year index linked Treasury yield fell from 2.35% in January to 1.92% as we write. These moves will cushion the economy somewhat.

There are also less easily quantifiable factors that have contributed to the mood shift. President Trump has made many pronouncements about introducing tariffs, making it difficult to keep up as he swings from imposing them and postponing their implementation. But what is different about the way he is going about introducing tariffs compared to his first Administration is that he is threatening to impose higher tariffs on goods from Canada, Mexico and Europe than he is on China. This is creating huge uncertainty.

The interlinkages between the US, Canada and Mexico are significant for many industries, not least the auto industry. It will be American companies and consumers who pay for the tariffs if they are imposed on any country, but particularly those imposed on Canada and Mexico.

The other new initiatives of Trump 2.0 are also creating uncertainty. The Department of Government Efficiency is making some wild claims for its success at discovering and eliminating “waste”. But firing people and shutting down agencies and programmes has risks given, as we have already seen, that some of these decisions have had to be reversed. The government spends over \$7,000 billion a year. For Musk to make a dent in that he will have to do a lot more than he is doing. For example, if he fired every Federal Government employee, he would reduce government spending by just over \$400 billion. That is just a 6% reduction in spending.

Trump also wants to slow illegal immigration from Mexico and deport more illegal immigrants. On the former there are signs of success. Border crossings are running at an annualised rate of 1 million, less than half the number who crossed in each of the last three years. Too early to tell if he is going to deport more than the 500,000 or so that have been deported each year in the last decade.

But this policy also creates uncertainty as it will effectively be a reduction in the labour force. For industries such as agriculture and construction it could lead to a need to raise wage rates to attract workers.

SUMMARY OF OUR VIEWS (CONTINUED)

These Trump policies threaten growth but tariffs in particular risk increasing inflation expectations. The good news is that so far inflation expectations remain anchored. This means the Federal Reserve will be able to cut interest rates (which the market expects them to do three times in 2025) if growth is indeed slowing significantly.

There is also good news in that investor sentiment has fallen significantly to levels that have previously been profitable buying opportunities.

So, we have not changed our asset allocation. We remain with a small overweight of equities and underweight of bonds.

EQUITIES (OVERWEIGHT)

The MSCI All Country World Index fell 1.9% in February but is up 2.2% this year.

The declines in market indices since the middle of February have made investors understandably nervous, particularly as the market leading stocks of the last two years have recently been leading the market down.

The US market has been lagging other markets this year and that trend has picked up in the first two weeks of March. With the “Magnificent 7” leading the US market downward that is not surprising. In the last month, Consumer Discretionary, Information Technology and Communication Services have been much the weakest sectors declining between 13% and 16%. The best performance has come from Health Care, despite the uncertainties associated with the possible policies being pursued RFK Jr, Utilities, Energy and Consumer Staples, the classic defensive sectors.

Value has outperformed growth around the world with Europe and the UK performing better. Japan has also outperformed. The best performance has come from Hong Kong and mainland China. A combination of factors are at play there but one is that the Deepseek AI announcement in January has highlighted how competitive Chinese companies are in technology. That President Xi met with technology business leaders, including Jack Ma, in a show of support has also helped sentiment considerably. Some investors have seen China as uninvestable in recent years but ironically that has changed even though that would have been difficult to predict with Trump back in the White House.

The market will be upended if we do see a recession in the US. But if we do not, the correction may well turn out to be a buying opportunity, despite all the macro uncertainty.

FIXED INCOME (UNDERWEIGHT)

The overall gilt total return index returned +0.8% in February and is up 1.7% this year.

We still see value in government bonds. We also see them as an important diversifier.

Short dated sterling credit is also attractive with yields of 5.5% on offer for an investment grade portfolio of bonds maturing within the next 18 months.

SUMMARY OF OUR VIEWS (CONTINUED)

ALTERNATIVES (NEUTRAL)

We believe Alternatives have an important role to play in diversified portfolios.

Absolute Return strategies can give exposure to an uncorrelated stream of returns giving diversification benefits. This sector has struggled in recent years, but well-run funds have attractive volatility dampening characteristics.

Real Assets such as property (both physical and intellectual), infrastructure (including transportation), commodities (such as gold) and other investments underpinned by physical assets offer a combination of income and capital return that is attractive. Many of the assets that produce income have inflation-linked cashflows.

CASH (NEUTRAL)

Even though savings rates have risen, cash still loses purchasing power quickly in any period of high inflation.

PART 1
POLITICS, POLICY, BONDS & CURRENCIES



TRUMP 2.0 POLICIES CREATE UNCERTAINTY: DOGE

The publicity generated by the Department of Government Efficiency. (DOGE) in the first weeks of Trump 2.0 has been extraordinary. Partly this is because of the media savvy of its leader, Elon Musk.

But it has created headlines for finding “waste” across the departments and agencies of the Federal government. And for giving employees cash if they resign. There have also been firings of workers in some Departments and Agencies.

The size of the task of restraining government spending though is enormous. The Federal government spent \$7.1 trillion in 2024 according to the National Accounts. That is \$7,100 billion.

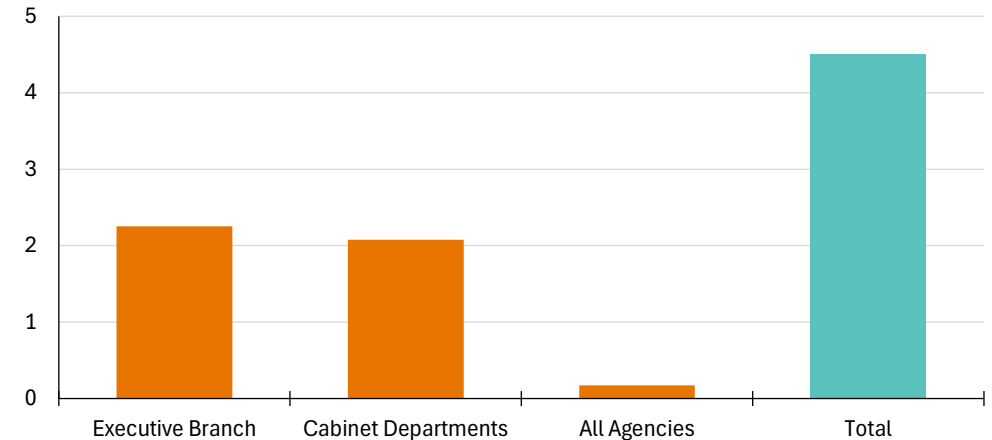
To put that in perspective, the 4.5 million Federal Government employees are paid a total of \$422.7 billion, an average salary of \$94,000 per annum. If Musk fired all of them, that would reduce government spending by just 6%.

This needs to be taken into consideration when Musk or Trump Press Secretary Karoline Leavitt wave a piece of paper around saying they have found an agency that is spending \$50 million on something they do not like.

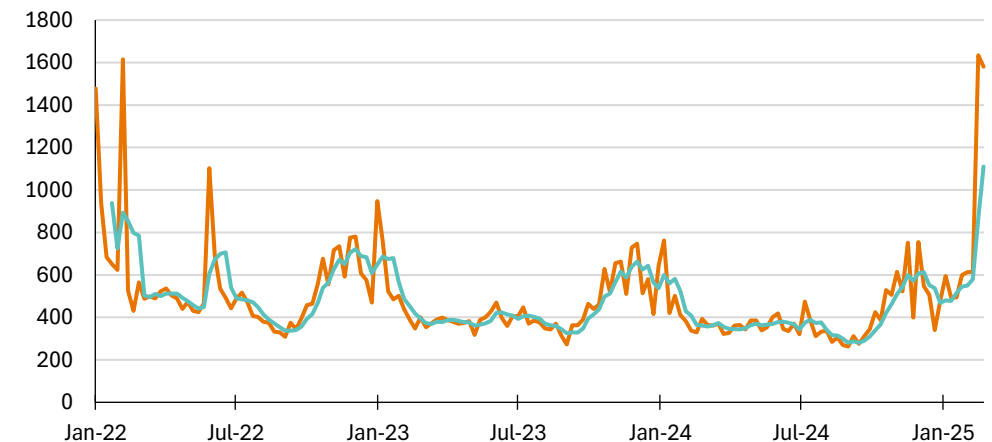
Having said that, if in fact DOGE does fire lots of people and reduces government spending more materially than one expects, then whatever the long-term benefits of that, in the short term it would be disinflationary for the economy and reduce growth.

Hence looking at initial unemployment claims of Federal Employees (the bottom chart) will be important. It has ticked up. Coincidence or DOGE? Time will tell.

NUMBER OF FEDERAL GOVERNMENT EMPLOYEES (MILLIONS)



INITIAL UNEMPLOYMENT INSURANCE CLAIMS FEDERAL EMPLOYEES



Source: www.doge.gov, Department of Labor. London & Capital Waverton. As at 28.02.25

TRUMP 2.0 POLICIES CREATE UNCERTAINTY: IMMIGRATION & DEPORTATION

The top chart shows the number (LH scale) of inadmissible or deportable foreigners who have left the country each fiscal year back to 1892. The data is also shown as % of the US population (RH scale).

Trump is starting at a low base relative to history so may well be that he increases the number somewhat. But more people left by this measure in the Biden administration (2.0 million) than did in Trump 1.0 (1.8 million).

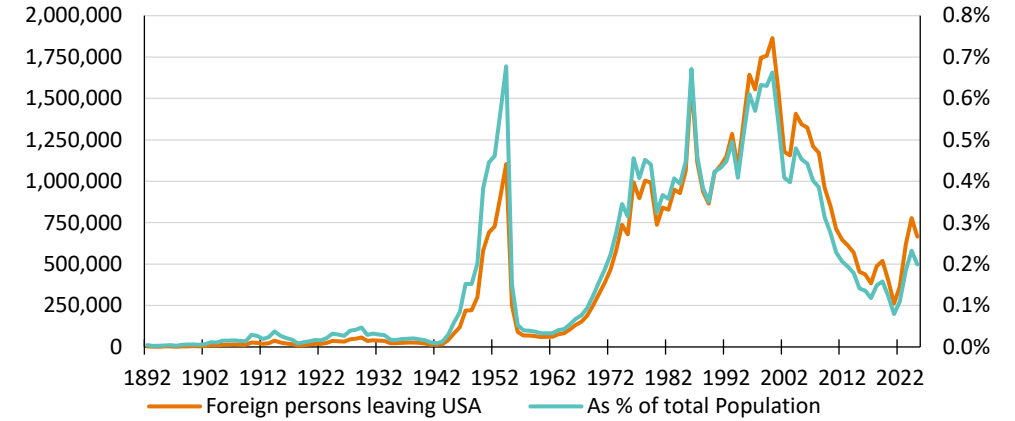
We can track the number of people removed monthly (last data is November 2024) so we can watch this closely. But it is possible that this is a classic "don't let the facts get in the way of a good story". One is sceptical this is going to impact wages, at least in the short term. If there is a material pick up, then it will impact industries such as construction and agriculture that have historically widely used cheap labour and have turned a blind eye to where people came from

But one accepts that Trump may be making some migrants think twice about crossing the border while this is getting so much publicity.

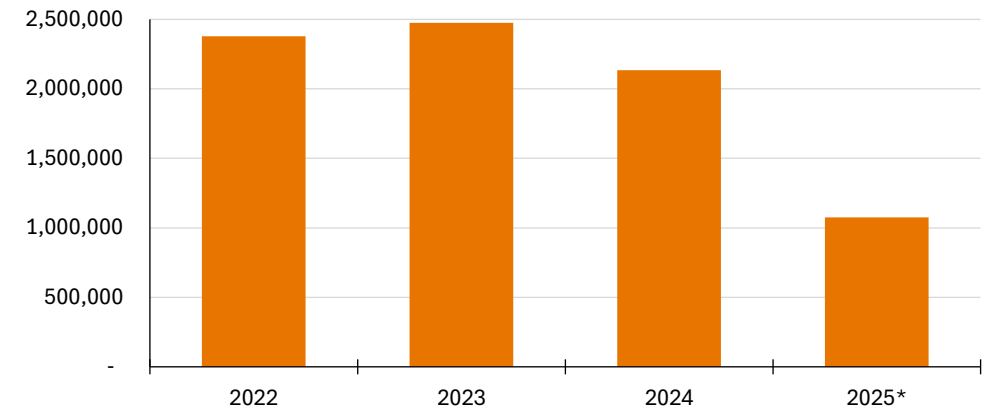
The bottom chart shows the number of people encountered at the south-west border by US Customs & Border Protection officers. After four months of the new fiscal year, crossings are running at less than 50% of the rate of the last three years on an annualised basis.

If this remains the case then Trump will be able to claim that he has had an impact, even though the crossings started to slow in the summer of 2024, before he was President.

INADMISSIBLE FOREIGNERS WHO LEFT THE USA, FISCAL YEARS 1892 – 2023



SOUTHWEST LAND BORDER ENCOUNTERS, FISCAL YEARS 2022 – 2025



Source: <https://www.cbp.gov/newsroom/stats/southwest-land-border-encounters> and <https://ohss.dhs.gov/topics/immigration/immigration-enforcement/immigration-enforcement-and-legal-processes-monthly>

* data annualised from first four months of 2025 fiscal year. As at 31.01.25

TRUMP 2.0 POLICIES CREATE UNCERTAINTY: TARIFFS

This chart shows the % of Federal tax revenues that come from tariffs. Under Trump 1.0 it increased from 1.9% in 2017 to 3.7% in 2018 but has been falling since then.

In Fiscal 2023 the US raised \$82 billion from tariffs out of an overall tax take of \$2,916 billion.

A large tariff on virtually all Chinese imports, then the revenue could be significantly higher than we have seen up to now. The US imported \$427 billion worth of goods and services from China in 2023. So a blanket 20% tariff would roughly double the current total revenue from tariffs.

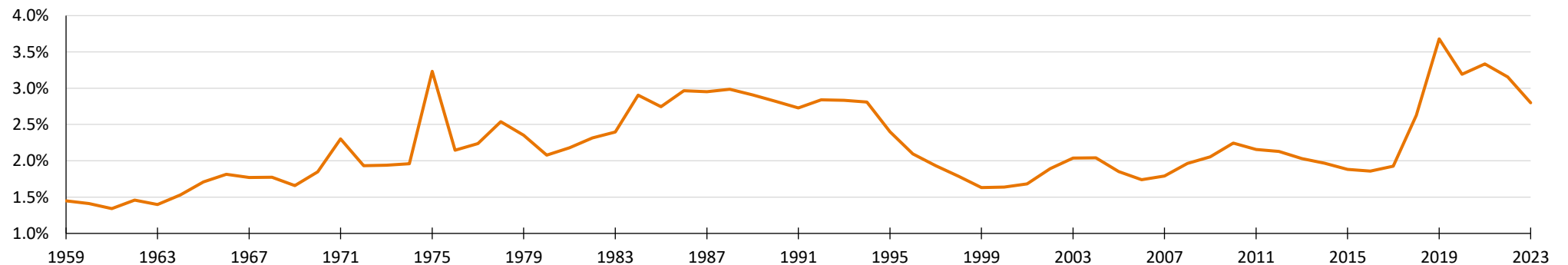
But tariffs are complicated because clearly China has retaliated by imposing tariffs up to 15% on US agricultural goods. The 25% tariff on Canada and Mexico has also been met with responses from both.

Canada imposed tariffs on around \$107bn of US goods. Mexico's response at the time of writing is unknown but there will be one.

Trump may also use tariffs as a broader foreign policy weapon. For example, Trump's enthusiasm for getting hold of Greenland could mean that he particularly focuses tariffs on Denmark. The US imported \$12bn of goods from Denmark in 2023, half of which was packaged pharmaceuticals.

All this creates uncertainty and could have implications for inflationary expectations and geopolitical risks.

US TARIFFS AS % OF FEDERAL GOVERNMENT TAX REVENUE FISCAL YEARS 1959 – 2023



Source: St Louis Federal Reserve, Bloomberg, London & Capital Waverton. As at 30.09.23

MARKET HAS BECOME WORRIED ABOUT A RECESSION

The New York Federal Reserve calculates a probability of a recession from the shape of the US yield curve. The probability goes up when the curve is inverted.

The curve is currently inverted from 10-years to 3-months which is regarded as the most robust way to calculate it.

But the probability is much lower than was the case in 2023 when this was one of many traditionally reliable indicators that gave a false signal. Indeed, there had always been a recession when the probability was as high as it was then.

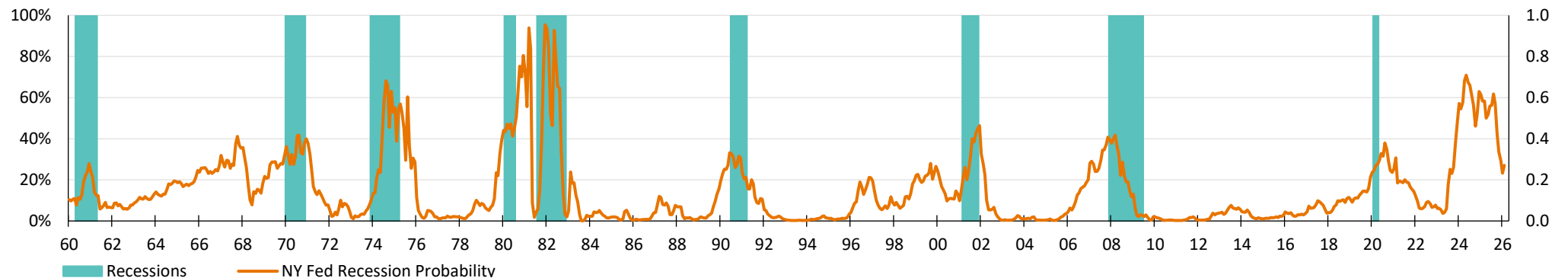
Despite that false signal, it is rational to look at the yield curve as an indicator of a future slowdown in the economy. When long rates are below short rates the market is suggesting that economic activity will slow in the months ahead and that the central bank is likely to cut interest rates.

The market is expecting the Federal Reserve to cut interest rates three times over the course of 2025. If expectations of a recession build, it is likely there will be more cuts than that.

The good news is that with a policy rate at 4.5% the Fed has room to cut, if needed, as long as inflation is not a problem. So far, expectations for inflation.

It will be important to see if that is still the case if and when tariffs are widely applied.

NEW YORK FED RECESSION PROBABILITY 1960 - CURRENT



Source: St Louis Federal Reserve, Bloomberg, London & Capital Waverton. As at 28.02.25

FISCAL POLICY WILL BE DOMINANT ISSUE IN 2025

This chart shows the US budget deficit as a % of US GDP. It is currently 7.2% of GDP. So far, the bond market has been relaxed about the likelihood of more supply of government bonds in the months and years ahead. But that could change in 2025 for two reasons.

Firstly, the Federal government debt limit has been reinstated as of 2 January 2025 at the level that includes all borrowing since the June 2023 suspension of the debt limit by Congress. So, it is a legal requirement that at some point this year Congress will have to raise the debt limit to permit more borrowing. The US Treasury can rely on its cash holdings for a little while before the limit needs to be raised but it is likely that the new Congress will have to deal with this issue by the summer of 2025.

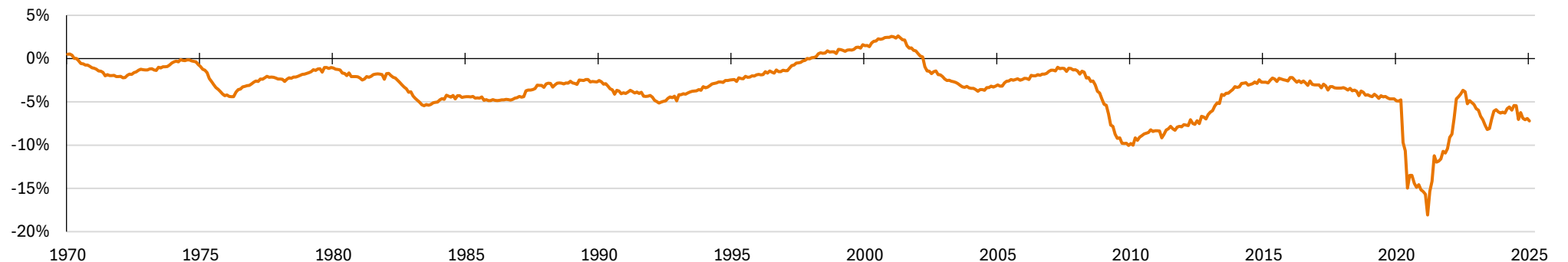
Secondly, the 2017 tax cuts for individuals and small businesses roll off at the end of 2025. If new legislation is not passed to renew them, then taxes will rise by over \$4 trillion.

That is looking likely to happen. Renewed tax cuts would be a positive for demand in the economy in the short term but will boost the deficit further in the medium term.

When Trump took office in 2017 the deficit was 3% of GDP. The current situation gives much less leeway for expansionary policy.

Could the bond vigilantes come out of hibernation in 2025?

US BUDGET DEFICIT AS % OF GDP 1970 - CURRENT



Source: Bloomberg, London & Capital Waverton. As at 31.01.25

FEWER RATE CUTS EXPECTED IN THE US AND UK

The top chart shows current expectations for the US Federal Reserve policy rate over this year and next and how those expectations have shifted since September 20th, the week the Fed cut rates by 0.5%.

There has been a material reduction in market expectations for monetary easing in the months ahead. There is a similar picture in the UK (bottom chart). In the US, three rate cuts are expected by the end of 2025.

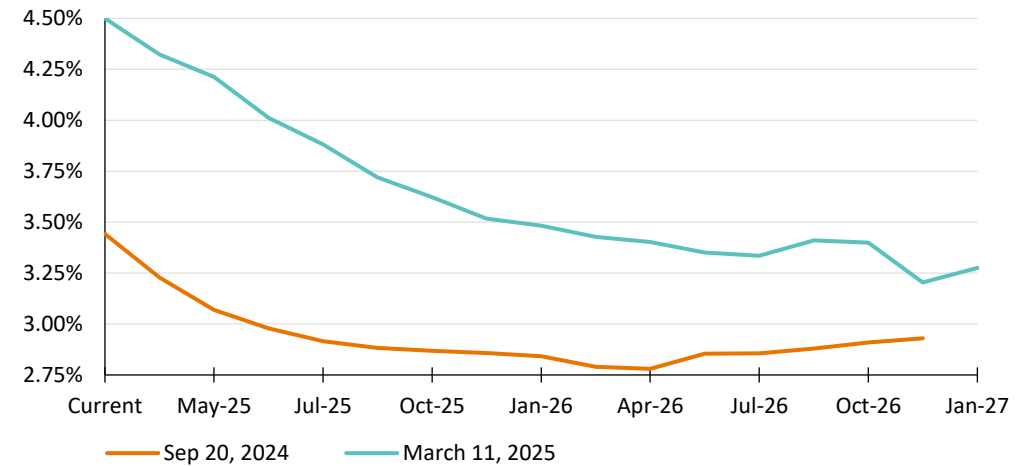
There is more concern about the likelihood of inflationary pressures returning after a stalling in the improvement in reported inflation in recent months and the potential actions of the Trump administration.

The imposition of high tariffs risk a jump in inflation. A presumption that tax cuts will be renewed at the end of this year also contributes to concern as, despite the headlines being made by the Department of Government Efficiency, meaningfully reducing spending is going to be challenging.

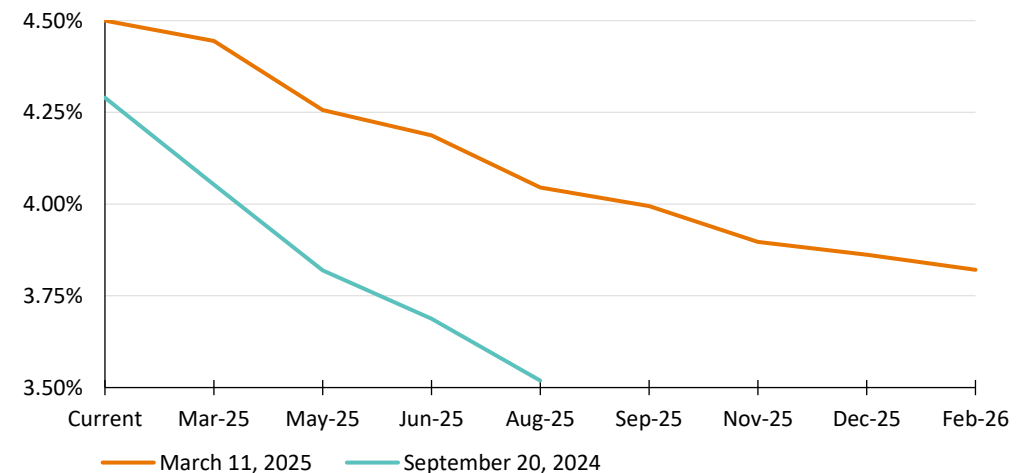
In the UK there is also an expectation of two rate cuts by the end of the year. Given the sluggish economy here it is possible that more may be forthcoming in the months ahead.

Market expectations for inflation are likely to be the critical thing to watch in coming weeks and months. If they do move up materially that will have a detrimental impact on markets.

IMPLIED US FED FUNDS RATE %



IMPLIED UK BASE RATE %



Source: Bloomberg, London & Capital Waverton. As at 11.03.25

TREASURIES RALLY ON GROWTH CONCERNS

The top chart shows how the yield on 10-year gilts and 10-year US Treasuries has evolved over the last two years. Bond yields rose after the Fed cut rates in mid-September, aided by some stronger than expected economic data, but have trended down since peaking in early January, with that down trend accelerating in the Treasury market since mid-February. Recent economic data in the US has been weaker than expected and the fear is that the combination of policies being embarked on by Trump (particularly tariffs but also potentially DOGE) will hurt growth further.

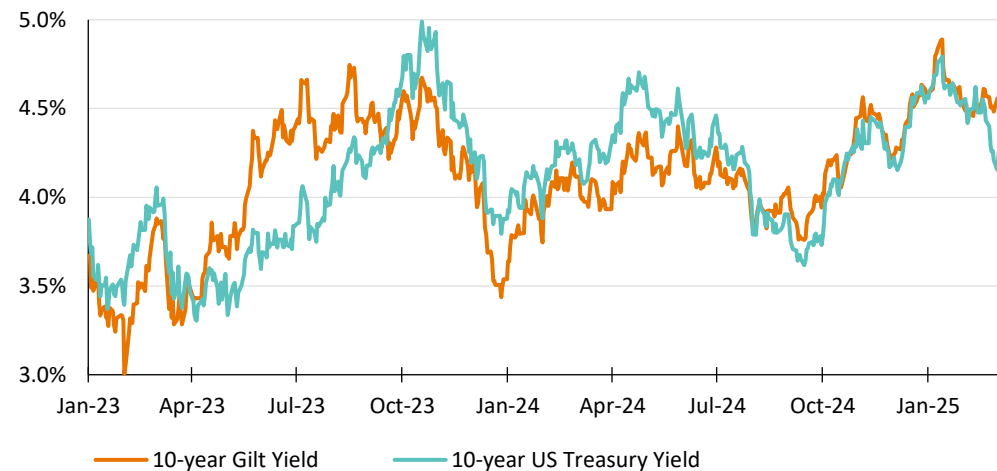
The bottom chart shows those same yields after deducting the current 10-year inflation swap rate in each market. The swap rate is one indication of market expectations for inflation over the life of the bond. Inflation swaps are priced on RPI in the UK so we deduct 1.2% from the swap rate to get an implied indication of expectations of CPI inflation (1.2% is about the long-term “wedge” between RPI and CPI inflation).

As the chart shows, both markets continue to offer, on this measure, a positive real yield. The rally in the last month or so in Treasuries has seen the real yield, as calculated this way, decline but at 1.8%, they remain attractive in our view.

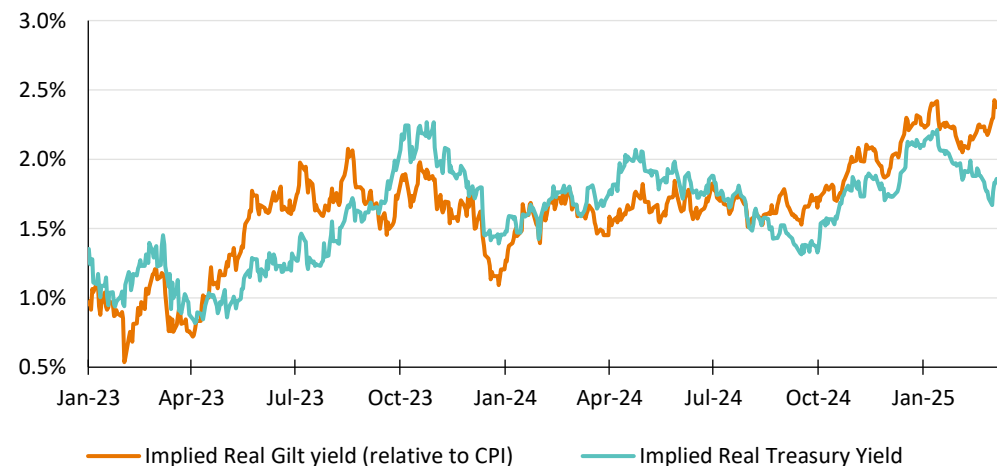
The inflation linked bond market is saying something similar in the US where the Treasury Inflation Protected Securities market is giving a positive real yield. The January 2034 TIPS yields 1.90%. The UK linker market is optically less attractive (the March 2034 linker yields 1.15%) but as this is based on RPI, the total return (thanks to RPI being higher than CPI) is similar between UK and US linker markets.

We still think there is value in government bonds given the positive real yields on offer.

US AND UK 10-YEAR BOND YIELDS (%)



US AND UK IMPLIED REAL 10-YEAR BOND YIELDS (%)



Source: Bloomberg, London & Capital Waverton. As at 04.03.25

INFLATION RATES HAVE DECELERATED AROUND THE WORLD

The peak for US inflation was in June 2022 at 9.1%. It is now 2.8%. The euro area peaked in October 2022 at 10.6% (now 2.4%) and the UK also peaked in October 2022 when RPI was 14.2%, and CPI 11.1%. RPI is now 3.6% and CPI is 3.0%.

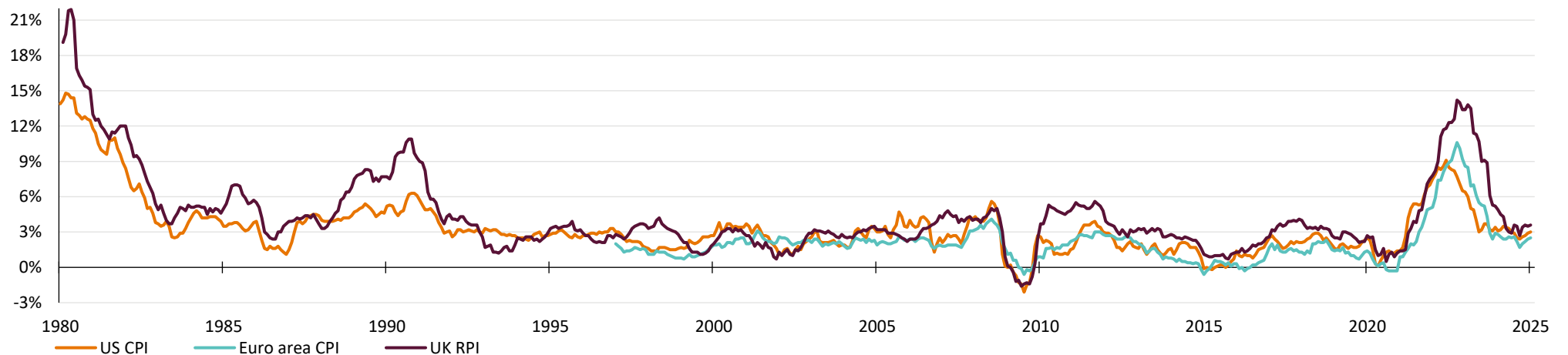
US core inflation (excluding food and energy) peaked at 6.6% in September 2022. It is now 3.3%.

There remain concerns about the inflationary impulse across the developed world. The improvement has stalled in recent months with inflation higher at the end of 2024 than it was in September 2024 in all three countries/regions.

With the impact of Trump's policies being debated some inflation risk premium may reappear.

However, for now, as the next charts show, the market is still somewhat sanguine about future inflation.

INFLATION (% CHANGE YEAR-ON-YEAR) 1980 – CURRENT



Source: Bloomberg, London & Capital Waverton. As at 28.02.25

EXPECTATIONS FOR FUTURE INFLATION REMAIN REASONABLY SANGUINE

The top chart shows the 5-year inflation swap rate which is one reflection of the market's view on future inflation. One can buy or sell the swap. If you think inflation will average more than the current price, you buy the swap and vice versa. The payoffs are roughly linear. If you buy at 2% and the outcome is 2.2%, you make about 10%.

The market remains sanguine about inflation over the next five years and indeed in recent weeks on both sides of the Atlantic, inflation expectations have been decelerating. This is good news.

But if future inflation actually takes longer to return to target that will be an issue for investors as it will almost certainly see a reversal upward in rate expectations.

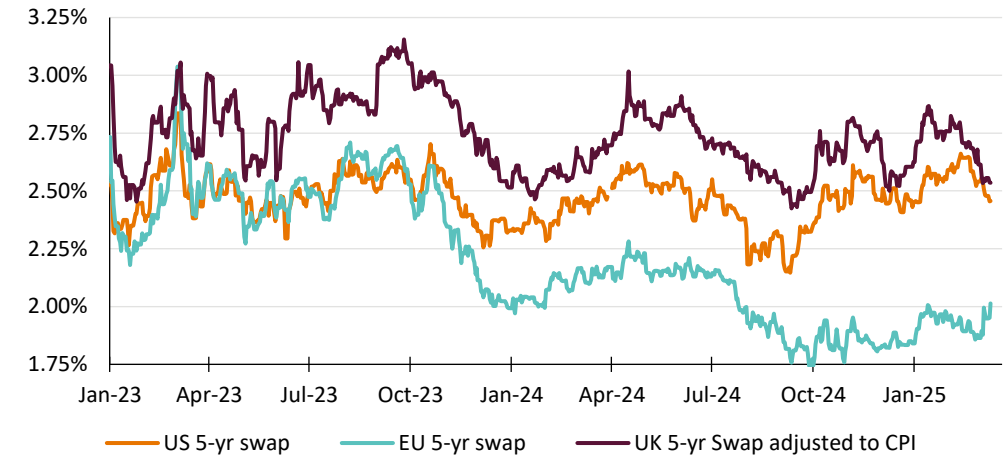
The bottom chart shows longer-term inflation indicators. Here the picture remains encouraging.

The green line is the 10-year US inflation swap and the dark blue line is the inflation rate calculated from the spread between five year nominal and inflation linked bonds five years forward. Both have been rangebound in recent months.

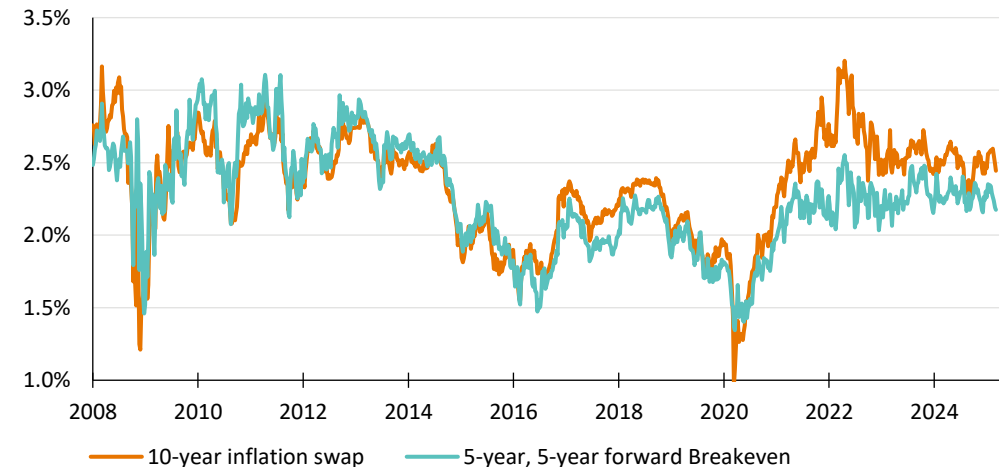
The general picture from both these charts is that the market remains pretty sanguine about future inflation.

One of the critical things to watch in coming weeks will be to see if the imposition of tariffs on a wide range of goods does anything to these measures of expected inflation.

5-YEAR INFLATION SWAP RATE (%)



LONG-TERM US INFLATION EXPECTATIONS



Source: Bloomberg, London & Capital Waverton. As at 11.03.25

THE BROAD COMMODITY COMPLEX HAS BEEN WEAK

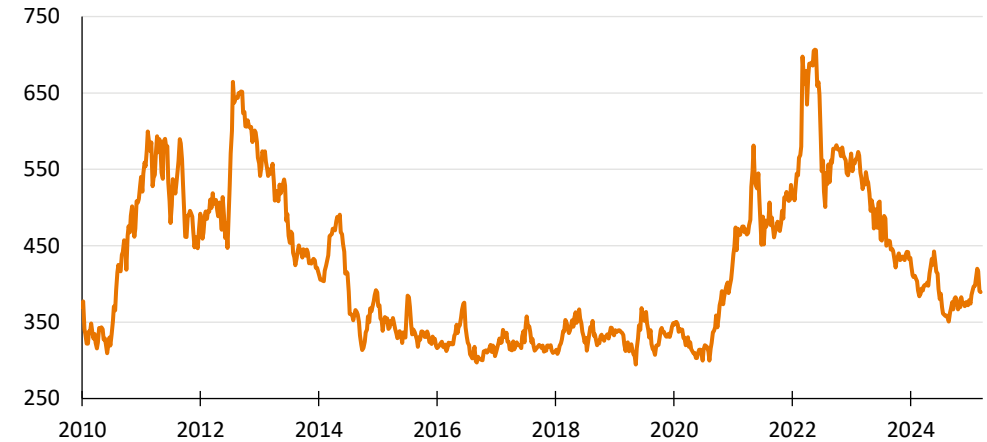
The broad commodity complex is in the doldrums.

Grain prices have been falling as fears of supply disruption from Ukraine, the bread basket of Europe, and Russia, have not materialised sufficiently to support prices.

The Industrial Metals index (bottom chart) has been range bound for the last eighteen months.

Demand from the People's Republic of China (PRC) is an important driver of industrial metals prices. There is little to suggest that recent efforts at stimulus are having much impact.

S&P GSCI GRAINS INDEX



S&P GSCI INDUSTRIAL METALS INDEX



Source: London & Capital Waverton, Bloomberg. As at 07.03.24

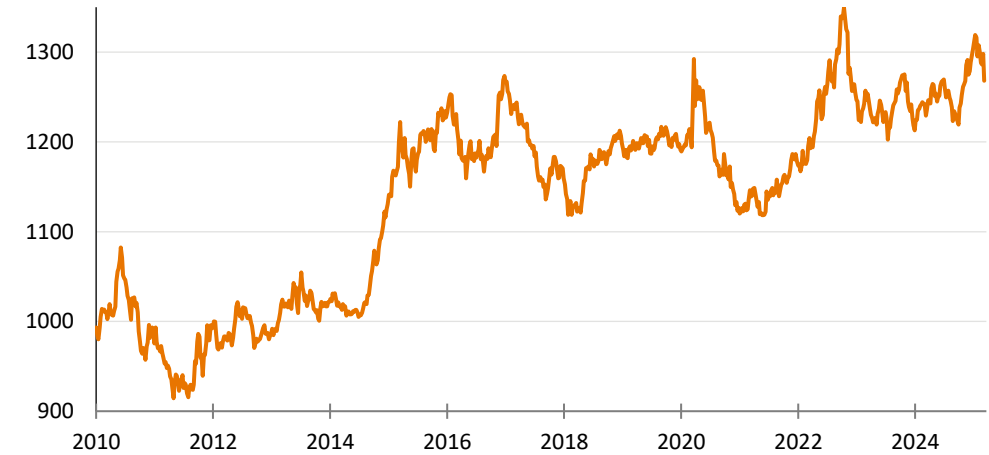
DOLLAR AT HIGH END OF ITS RANGE

The top chart shows a trade weighted dollar index. It has strengthened in the run up to and post the Presidential election. This also coincides with the shift upward in expectations for where future policy interest rates are going.

The bottom chart shows that an index of emerging market currencies. This index is weighted by the weighting of each country in the MSCI Emerging Market equity index, so China is the biggest component.

The election of Trump has rationally pushed the US dollar up against EM currencies, including the renminbi which is at 7.23 to the dollar, up from 7.10 at the time of the election. It is at the top end of its range against the dollar.

TRADE WEIGHTED US DOLLAR (BBDXY)



MSCI EMERGING MARKET CURRENCY INDEX



Source: London & Capital Waverton, Bloomberg, MSCI. As at 07.03.25

STERLING STILL RANGEBOUND AGAINST THE EURO, BUT AT THE HIGHER END

Although there has been a lot of comment about the UK in crisis, as the chart below shows, sterling is still trading toward the top end of its range against the euro since 2016.

We continue to think that the exchange rate versus the euro is a better measure of the market view of UK specific risks than the sterling/dollar rate.

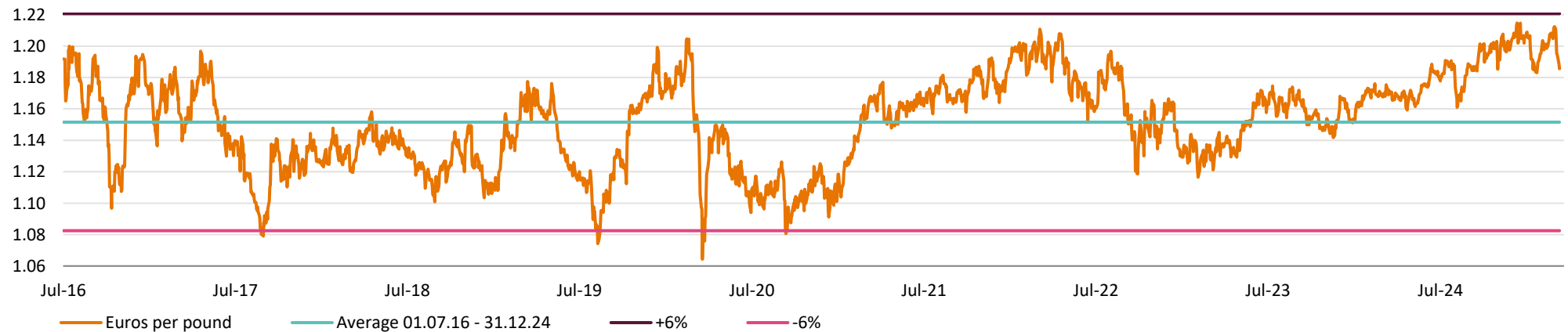
The chart shows the number of euros per pound since 1st July 2016. The average exchange rate since then is shown as the teal line and we show a range 6% either side of that average.

We use 6% as that was the range sterling was allowed to trade against its DM2.90 central rate when it was in the Exchange Rate Mechanism (ERM). Famously sterling was forced out of the ERM in September 1992 when it was unable to hold within that range.

We note that over the period shown (over 2,200 trading days), sterling has only been out of a 6% trading range for ten days.

For now, there is little sign of an elevated UK sovereign risk premium on this measure at least. If anything, the market is more worried about the euro area.

EUROS PER POUND (01.07.2016 – CURRENT)



GOLD AT A RECORD HIGH

As of the end of January 2025, gold is at a record high in US dollars and in sterling terms.

With all the uncertainty highlighted on previous pages of this presentation, we are of the view that gold has a role to play in diversified portfolios.

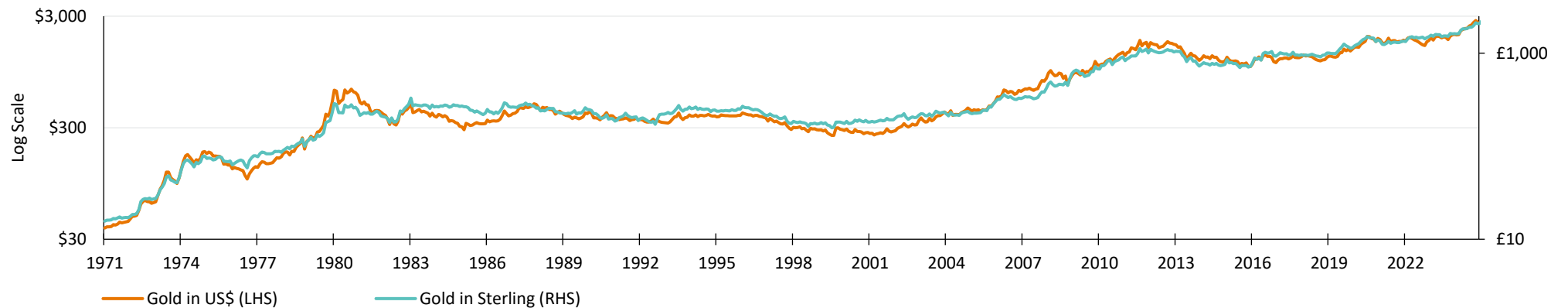
Gold benefitted from the exceptional monetary policy in evidence from 2008 to arguably 2021. With zero or even negative nominal interest rates the opportunity cost of owning gold had never been lower.

In recent months, the rally in gold appears to be based on buying by central banks around the world, including in China. It is also possible that gold has benefitted as a hedge against any reappearance of inflation.

There is also the possibility that the Trump Administration will revalue its gold holdings. It carries them in the accounts at a value of \$42.22 per ounce. The current price is \$2,882. The value of the gold held by the US government is \$11bn at the \$42 valuation. It would be \$750 billion at the current price. That could be used to finance a sovereign wealth fund or just be used to shore up the health of the government balance sheet.

There are lots of devils in the detail of doing that though so count it as unlikely. More important in the short term will be whether the demand from central banks for gold continues.

GOLD PRICE PER TROY OUNCE IN US DOLLARS AND IN STERLING – 1971 - CURRENT



PART 2
EQUITIES & CREDIT



2025 EARNINGS GROWTH ESTIMATE +12% GLOBALLY AND +14% FOR THE US

For 2025 the consensus numbers remain very robust at +12% for the World index and +14% for the US.

It remains the case that there are valuation excesses in some of the leading companies in the US but valuations in the rest of the US market, and in the rest of the world, are not stretched.

EARNINGS PER SHARE CALENDAR YEAR GROWTH RATE

REGION	PE NTM	RELATIVE	GROWTH RATE		
			2024	2025	2026
World	18.2	-	+9.8%	+12.7%	+8.6%
US	22.0	121%	+10.2%	+14.2%	+12.0%
Europe ex UK	15.1	83%	+8.4%	+11.1%	+10.4%
UK	12.1	67%	+5.2%	+10.7%	+8.4%
Japan	13.8	76%	+10.9%	+8.5%	+9.0%
Asia Pac ex Japan	12.9	71%	+9.4%	+13.4%	+3.0%
Latin America	8.2	45%	+39.7%	+10.2%	+7.6%
Emerging markets	14.0	77%	+8.7%	+11.4%	+10.5%
World ex USA	13.7	75%	+9.1%	+11.0%	+6.2%

Source: MSCI, FactSet, London & Capital Waverton. Data as at 28.02.25

STOCK MARKET VALUATION IN LINE WITH RECENT RANGES

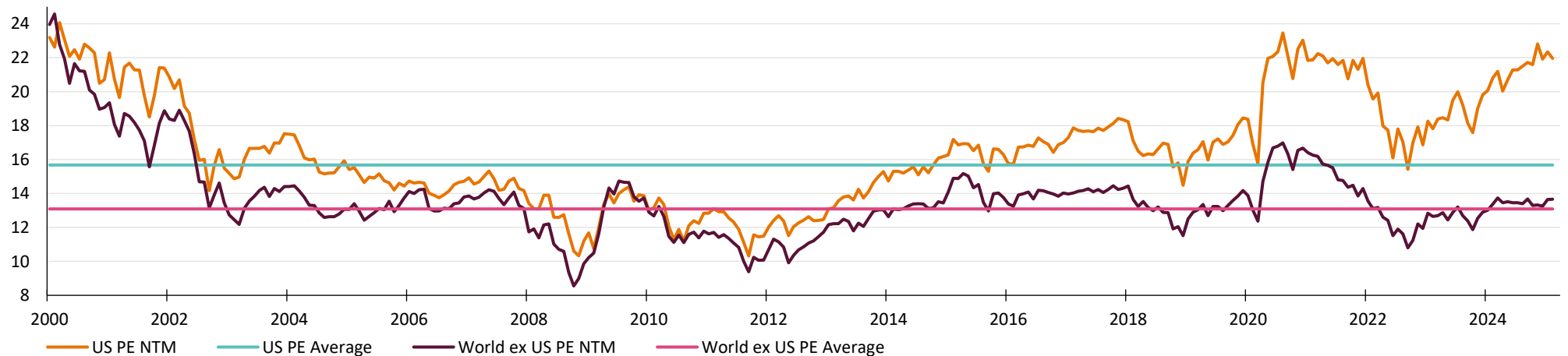
The PE ratio for the US market (solid orange line) is 22.0 times.

It is again above its 20-year average of 15.7 times (the teal horizontal line).

The World outside the US now trades at 13.7 times earnings, a little above its 20-year average of 13.1.

There is always uncertainty about the EPS these valuations are predicated on but particularly outside the US there is a reasonable amount of that uncertainty priced in.

MSCI US AND MSCI GLOBAL EX US PRICE-EARNINGS RATIO BASED ON NEXT 12 MONTHS EARNINGS



Source: MSCI, FactSet, London & Capital Waverton. As at 28.02.25

US MARKET NOT AS EXPENSIVE AS HEADLINE VALUATION SUGGESTS

Although the valuation of the US market is elevated in absolute terms and relative to its own history, a small number of large companies in the index are the cause of that. The narrowness of the leadership in the market in the last two years has exacerbated that.

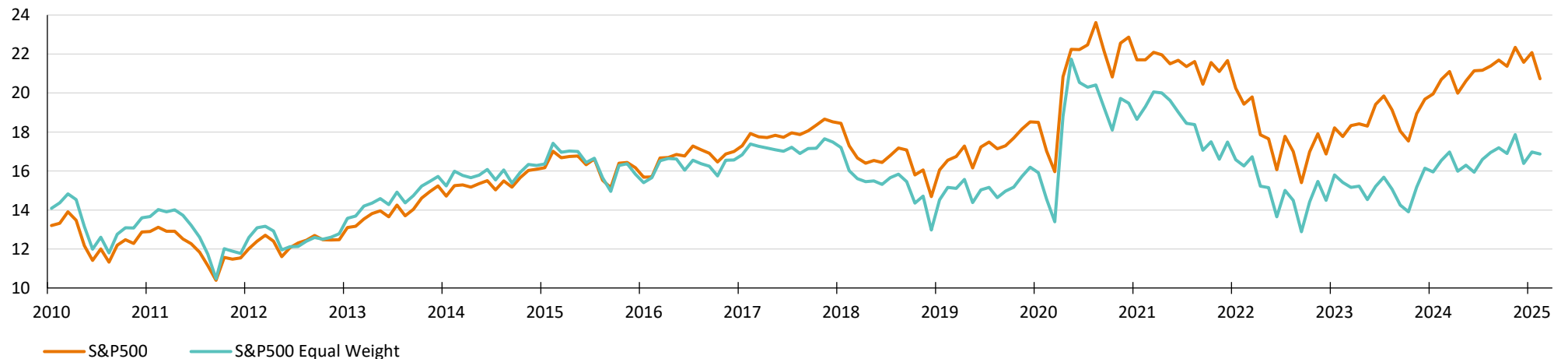
This chart looks at the price/earnings ratio of the index (orange line) and the PE of an equally weighted version of the S&P500 index, both on forward earnings.

The former is at 21 times, the latter is at 17 times.

That is the widest discount seen in recent years. Which is why we have still been able to find value in the US market and have added US stocks to our Global Recommended Portfolio in recent months.

It is important to bear this in mind as it suggests that while elevated valuations pose risks to a few of the largest stocks in the index, the rest of the market is trading at reasonable levels. The 20-year average PE for the US is 15.7 times so the equally weighted index is only slightly elevated relative to that.

S&P500 INDEX AND S&P500 EQUAL WEIGHTED INDEX, PRICE EARNINGS RATIO 2010 – CURRENT



Source: Factset, London & Capital Waverton. As at 11.03.25

US PROFITS AS % OF GDP REMAIN RESILIENT

This chart shows pre-tax profits of corporate America relative to GDP through Q3 2024, the most recent data available. This profit series shows aggregate profits across the whole economy and shows them in US dollars, not as earnings per share.

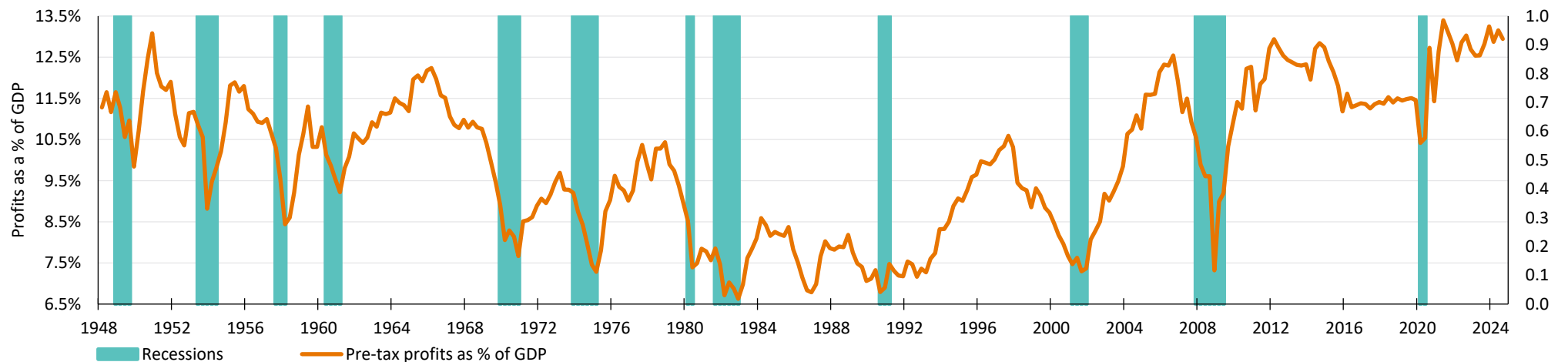
Consequently, this series is not susceptible to financial engineering via such things as share buybacks to boost earnings per share. It is a proxy for profit margins. In every recession except 1982, profits were falling as a % of GDP before it.

But on this measure profits have been resilient in recent quarters. Profits are below the cyclical peak as % of GDP which was 13.4% in Q2 2021.

The profit data has just been given a boost by the annual update of the National Income Accounts. Profits were increased by \$550bn combined in the last three years which equates to an average of over 5% per annum.

The effect of this is to eliminate the drop in profits as % of GDP in 2023 that had added to the indicators suggesting an economic slowdown was likely. Now, this another indicator suggesting a recession in the near term is unlikely, and indeed confirms that the health of the corporate sector is genuinely robust.

US PROFIT CYCLES AND RECESSIONS (%)



Source: MSCI, FactSet, London & Capital Waverton. As at 30.09.24

UK MARKET HAS BEEN A DISAPPOINTING ONE FOR MANY YEARS

The UK stock market has significantly underperformed the World index in recent years.

Between 2001 and 2014 there was not a lot of difference between the two.

But from May 2014 to October 2020, the UK market underperformed by 49%. It had a better time in 2022 but it has resumed underperformance in the last two years.

One of the issues for the UK is that it has few technology or communication service companies that have been the market leaders in recent years. They are a combined 4% of the UK market.

Another issue is that recently the weakest sectors in terms of earnings growth have been energy, healthcare, materials and financials. They are a combined 52% of the UK market.

It will be interesting to see if the recent rotation out of technology related sectors produces a better performance from the UK.

MSCI UK RELATIVE PERFORMANCE TO MSCI ALL-COUNTRY WORLD, BOTH IN STERLING



Source: MSCI, Bloomberg, London & Capital Waverton. As at 07.03.25

JAPANESE MARKET HAS SEVERAL TAILWINDS

The Japanese stock market has been aided by a number of tailwinds in recent years. The market first hit new all-time highs in March when it finally (as measured by the Nikkei 225 Index) closed above its 29 December 1989 previous high.

Macro factors have played a role. The Bank of Japan has bucked the trend of other developed world central banks by, coincidentally also in March, only ending negative policy rates recently. The policy rate is at +0.25%. The apparent ending of deflation enabled this to happen although policy rates obviously remain very negative in real terms.

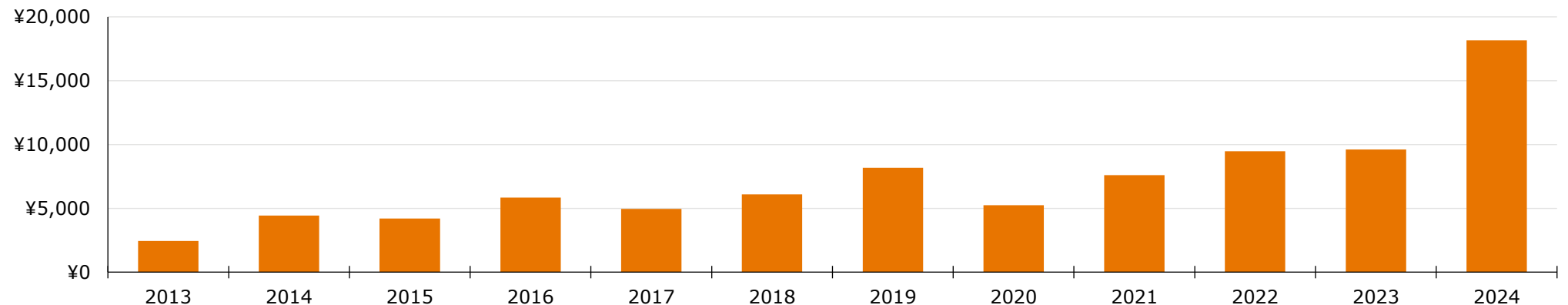
But there have also been significant changes to corporate governance including a sharp increase in the number of independent directors on Boards. Shareholders have benefitted directly from a pick up in the number of buybacks done by Japanese corporates.

This chart shows that buybacks were at a record level in 2024, 89% above the level of last year.

On top of that, foreign investors have been more bullish and have also been buying the market. We continue to like a number of Japanese companies and are overweight in aggregate in our global equity portfolios.

These secular tailwinds make us confident that select Japanese equities have an important role to play in equity portfolios.

JAPANESE CORPORATE SHARE BUYBACKS 2013 – CURRENT IN MILLIONS OF JAPANESE YEN



Source: Mizuho, Bloomberg, London & Capital Waverton. As at 31.12.24

US INVESTOR SENTIMENT LESS BULLISH

This is the weekly survey of its members done by the American Association of Individual Investors. The chart shows the % of respondents who are bullish among those that express a view (so it is Bulls as a % of Bulls plus Bears).

This could not be a simpler sentiment measure, but it is worth knowing about.

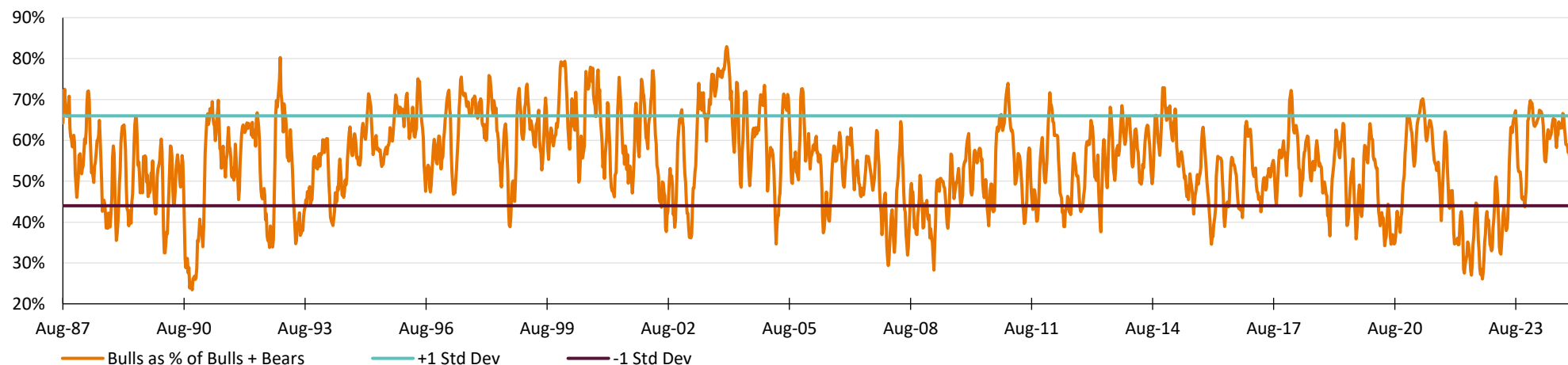
The two horizontal lines are showing one standard deviation above (teal line) the average level and one standard deviation below (purple line).

If you buy the market when the orange line is below the purple line your average return in the next year is +15%.

If you buy the market when the orange line is above the teal line your average 12-month return is +6%.

This sentiment measure has followed the market by staying at the top end of the bullish range in recent weeks. Don't think one could describe as investor sentiment as euphoric, but there may be a little complacency around.

AMERICAN ASSOCIATION OF INDIVIDUAL INVESTORS SURVEY, BULLS AS % OF BULLS PLUS BEARS



Source: AAI, Bloomberg, London & Capital Waverton. As at 06.03.25

CORPORATE BALANCE SHEETS YET TO SHOW REAL STRESS

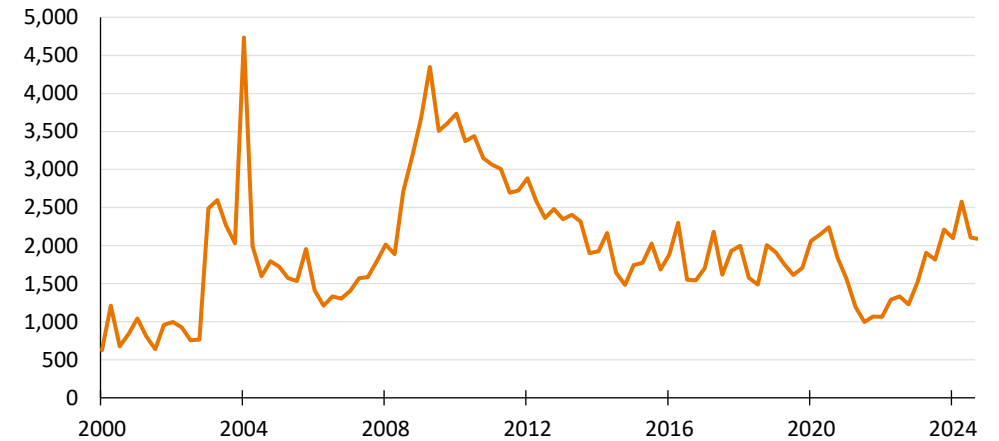
The top chart is a quarterly series showing the number of US corporate bankruptcies (officially called “Chapter 11” filings). It hit its lowest level for 18 years in Q3 2021.

It has moved up since then but has declined in both Q3 and Q4 2024.

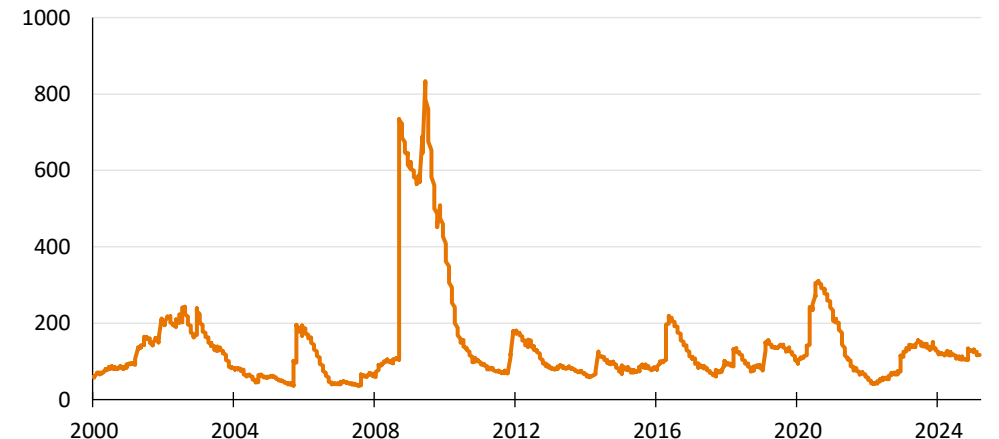
The Bloomberg Index in the bottom chart is of economy wide US bankruptcies and takes into account the size of the bankruptcy as well as the number of them. Hence there were more big bankruptcies in 2009-10 than in 2003-04. That index is at historically very low levels.

It remains the case that corporate balance sheets are holding up well in the face of higher interest rates.

US BANKRUPTCY FILINGS (2000 TO CURRENT, QUARTERLY)



BLOOMBERG US CORPORATE BANKRUPTCY INDEX (2000 – CURRENT, WEEKLY)



Source: Bloomberg, London & Capital Waverton. As at 07.03.25

CORPORATE CREDIT MARKETS BULLED UP

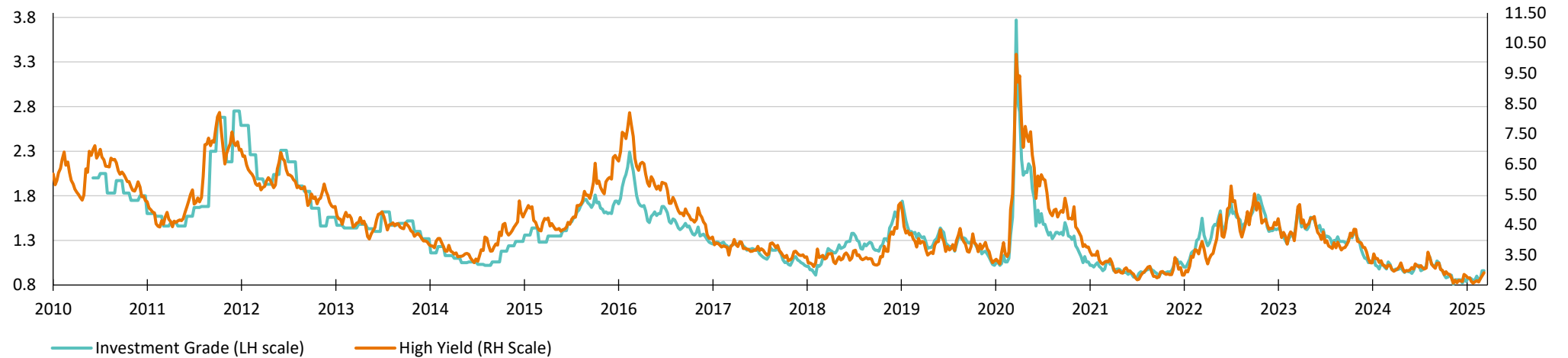
Credit spreads have tightened as the risk-on rally continued in recent weeks.

Spreads will widen if there is a risk of higher inflation and tighter monetary policy for longer than currently expected.

We remain of the view that credit spreads reflect some investor complacency.

Hence our lowest allocation to credit in our bond funds since their inception.

US CORPORATE BOND SPREADS (%)



Source: Markit, Bloomberg London & Capital Waverton. As at 07.03.25

CORPORATE BONDS, S&P500 EARNINGS YIELD & T-BILLS HAVE SIMILAR YIELDS

The Moody's Baa yield (a benchmark for the investment grade market) has been above the earnings yield of the S&P500 Index at end of each month since January 2023. At the end of February 2025, the numbers were 5.9% versus 4.3%.

The last two periods when this was the case were the run up to the Dotcom peak in 2000 and its unwind. Then this happened again during the Global Financial Crisis of 2007-09.

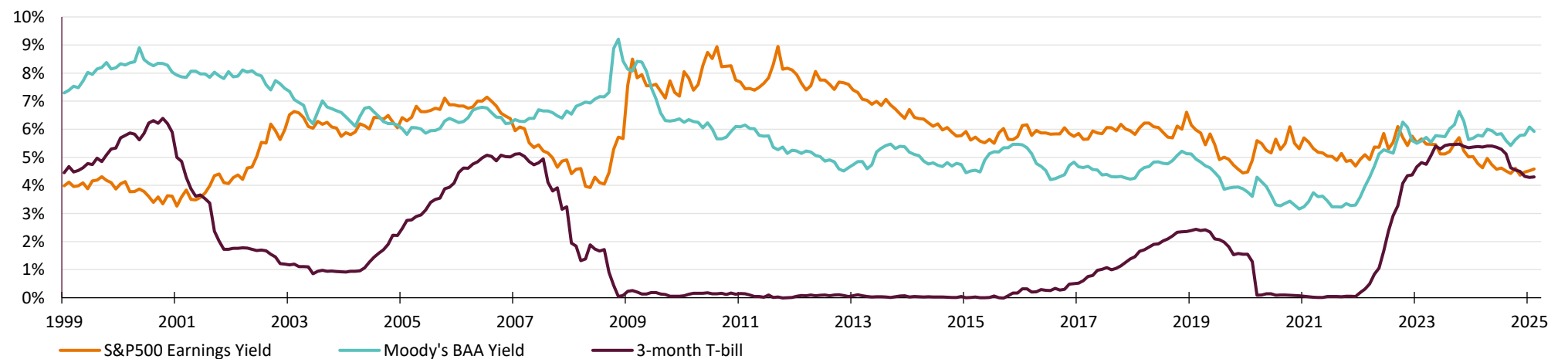
Normally it would be perceived that equities had some valuation challenge from corporate bonds when this is the case but in 2023 both gave good returns.

That the earnings yield and the Baa yield have both moved down over the summer reflects the strength of both markets.

The grey line is the 3-month Treasury bill rate which is currently 4.3%, only slightly below the S&P500 earnings yield. Cash remains the most competitive it has been to equities since 2001.

This chart also suggests it is rational for investors to be more favourably disposed toward cash today than has been the case since pre the GFC.

MOODY'S CURRENT BAA CORPORATE YIELD, S&P500 FORWARD EARNINGS YIELD, 3-MONTH TREASURY BILL YIELD (%)



Source: Moody's, Bloomberg London & Capital Waverton. As at 28.02.25

WEAKNESS OF CHINESE CURRENCY NEEDS TO BE WATCHED

The Rmb has been weak since the US Presidential election in early November.

As my colleague Benjamin Hall points out, in China, despite consistent messaging on a commitment to stimulus, including directly from Xi, investors have reverted to “I’ll believe it when I see it” mode. These conditions led to broad based weakness across Asian markets and currencies during the quarter.

As Ben also says, it was positive to see some constructive data points from the real estate market. Primary transaction volumes have been on an uptrend since the government’s policy changes three months ago, while inventory levels have been declining given the drop in new project starts. So far, the real estate downturn hasn’t pushed too many homeowners into negative equity, due to China’s low LTV ratios and the huge deposit build up since COVID. Putting a floor under the real estate market at this stage to avoid that happening (and the consequent asset impairments for the banking system) remains critical. The government seems to be proceeding with a targeted and incremental stimulus response. They appear to be focusing on the underlying faults in the system, notably local government debt and the real estate market; investors seem to still wish for a bazooka to be fired at the symptoms (i.e. weak consumer spending).

The Taiwan dollar is stable, despite the scaremongering headlines about Taiwan that appear regularly. We continue to remain sceptical about the PRC conducting a military operation against Taiwan. But the sabre rattling around the issue will continue.

We will continue to watch the Taiwan dollar to see if the market is taking any threat from Beijing more seriously than it apparently does, quite reasonably, at the moment.

RENMINBI PER US DOLLAR



TAIWAN DOLLAR PER US DOLLAR



Source: Bloomberg, London & Capital Waverton. As at 07.03.25

PART 3

OUR APPROACH TO INVESTING RESPONSIBLY



OVERVIEW OF RESPONSIBLE INVESTMENT AT LONDON & CAPITAL WAVERTON

Signatory of:



LONDON & CAPITAL WAVERTON RESEARCH PROCESS

- Integration of ESG factors into fundamental analysis and decision-making
- Incorporated into research process across all asset classes
- Specialist thematic, sustainable and impact fund research



ETHICAL RESTRICTIONS

Client-specific ethical exclusions can be applied at the portfolio or fund level

ENGAGEMENT AND VOTING

- Direct engagement with company management
- Collaborative engagement activities
- Proxy voting by Glass Lewis

RESPONSIBLE STEWARDSHIP OF CLIENTS CAPITAL

We aim to identify responsible allocators of capital ensuring business resilience and long term financial sustainability

How we incorporate ESG

- Integrated approach to the assessment of ESG factors
- Detailed fundamental analysis avoids greenwashing
- Mitigates poor data quality and inconsistent third-party ESG ratings
- Focus on engagement over an exclusion/divestment strategy
- Identify those successfully adapting to ESG opportunities/risks
- Acknowledge when ESG risks are integral to transition solutions
- Pragmatic approach focused on high or improving ESG standards

The advantages of our investment approach

- **Global:** largest universe of investment opportunities
- **Direct:** greater transparency around ownership
- **Active:** flexibility to avoid areas at risk of capital loss
- **Concentrated:** in-depth identification / monitoring of risks
- **Experienced team:** library of knowledge is an advantage
- **Engaged:** long-term relationships create a two-way dialogue
- **Strong ESG outcomes:** natural result of our approach

Signatory of:



IMPORTANT NOTICE

The value of investments and any income from them can fall as well as rise and neither is guaranteed. Investors may not get back the capital they invested. Past performance is not indicative of future performance. The material is provided for informational purposes only. No news or research item is a personal recommendation to trade. Nothing contained herein constitutes investment, legal, tax or other advice. This document does not represent primary research; it provides the views of the London & Capital investment team examining the fundamental background, economic outlook and possible effect on asset markets. This document is not an invitation to subscribe, nor is it to be solely relied on in making an investment or other decision. The views expressed herein are those at the time of publication and are subject to change. Correct at time of going to press. © London and Capital Asset Management Limited. All rights reserved.

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