

# GLOBAL OUTLOOK

May – June 2025

This document should be used as a guide only. It is based on our current view of markets and is subject to change.

## 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 Trump administration remains the dominant driver of the news cycle. Since the April 2nd "Liberation Day" announcement of a 10% tariff on all imports and higher tariffs aimed at countries with surpluses in trade with the US, we have seen a variety of changes to those policies that has persuaded that market that the end result will be a manageable increase in tariffs that will not produce a recession nor produce persistent inflation. The most important policy revisions have been the 90-day pause in the elevated tariffs for most countries announced on April 9 and then the 90-day pause in tariff increases imposed by the US and China on each others imports.

It is good news that we have stepped back from policies that were likely to produce significantly negative economic consequences. But we are still in a far from stable environment. The US is imposing a 30% tariff on Chinese imports during the 90-day pause, down from 145% but still elevated. China is imposing a 10% tariff on US imports, down from its threatened 125%. These policies will have less negative consequences than those announced in April but they are still challenging for businesses and consumers. An environment in which policy can fluctuate this wildly is not conducive to making business investment decisions. And consumers will see prices for impacted goods rise, as highlighted by Walmart on 15th May.

Despite the considerable uncertainty that is obviously with us, there has been good news in that economic data has not deteriorated and indeed the news on inflation has been benign. We continue to see the market expectations for future inflation to be the most important economic indicator. Partly this is because if inflation stays well anchored it means that Central banks can respond to any signs of weakness in economic data.

So far, those expectations, as measured by 5-year inflation breakevens or 5-year inflation swaps, are not suggesting a serious spike. The breakeven is at 2.4%, exactly the level it was at the end of 2024. The swap is up to 2.6% from 2.5% at the turn of the year but this is not yet in worrying territory. But any further upward moves from here would be concerning.

The stock market has recovered strongly from its low close on April 8<sup>th</sup> but bond yields have been rising this month. They are below their highs in January, on both sides of the Atlantic, but bond yields need to be watched closely given the above-mentioned inflation concerns but also because there are a number of fiscal policy challenges for American lawmakers in the months ahead. Trump wants a "Big Beautiful Bill" encompassing tax cuts and raising the debt ceiling that will be reached in July or August. But the Republicans have only a majority of three seats, coincidentally, in both the House and Senate. Passing this bill, initially in the House, is not guaranteed. We should know more by the end of May. But there is a possibility that markets will get jittery if the bill is passed (as it almost certainly raises the budget deficit which is already at 7% of GDP). And markets could get jittery if the bill is not passed as by the end of the year the government will run out of money and in January 2026 the 2017 tax cuts passed by the first Trump administration will end without being re-legislated which would be a \$4+ trillion tax increase which will be very negative for the growth outlook.

On top of that, the vagaries of policymaking by the Administration, the pandering to traditional foes of the US and the hardball tactics being used to traditional friends of the US mean that some believe that investors will want to own fewer dollars, both in terms of the currency, bonds and equities. We are sceptical that things will be taken that far, but overall the picture is one where extreme uncertainty is present. Hence our remaining broadly with a broadly neutral asset allocation.

# SUMMARY OF OUR VIEWS (continued)

## **Equities (neutral)**

The MSCI All Country World Index fell 2.5% in April and is down 6.6% this year.

Commentary from Head of Equities, Jen Fisher:

The tone for markets was dictated by Trump's Liberation Day tariff announcement on 2nd April, followed by further evidence of his cavalier approach to US policy and trade policy in particular. Volatility spiked and US policy headlines drove market sentiment on an almost daily basis.

The uncertainty this has injected into both corporate and consumer behaviour is already distorting economic data and will continue to do so over the near/medium term.

US and global growth expectations are moving lower and inflation expectations in the US in particular remain sticky given the anticipated impact of tariffs. The decline in oil prices, however, potentially provides a disinflationary element.

Against this backdrop, we saw a month of two halves, with a defensive bias evident over the first two weeks and a more value cyclical bias over the latter two weeks as Trump adopted a more constructive tone towards tariff negotiations, and with earnings results and guidance proving relatively resilient so far.

It is important to distinguish, however, between Corporate America and Politics America and premature to be calling for the broad-based demise of the US corporate sector, which still accounts for ~64% of the MSCI ACWI and will continue to offer investors the greatest breadth and depth of investment opportunity in the world for the foreseeable future. For reference, the next largest single equity market is Japan (5% of the index).

## **Fixed income (neutral)**

The overall gilt total return index returned 1.8% in April and is up 2.3% 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.

## **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.

Risk warning: The above should be used as a guide only. It is based on our current view of markets and is subject to change. As at 21.05.25

Part I POLITICS, POLICY, BONDS & CURRENCIES

## TRUMP 2.0 POLICIES CREATE UNCERTAINTY: TARIFFS

This chart shows the effective tariff rate on all US imports since 1790.

The latest iteration of Trump's tariff plans means that the average tariff rate is estimated by The Budget Lab at Yale to be 16.4%. The 90-day pause on the so called Reciprocal Tariffs, and the postponement of the elevated tariff on Chinese goods, has reduced the tariff rate from 24% a month ago. The current estimated tariff is the highest since 1936 in the wake of the Smoot Hawley Act of 1930.

In Fiscal 2023 the US raised \$82 billion from tariffs out of an overall tax take of \$2,916 billion. The potential revenue from the new level of tariffs could be as high as \$600 billion. But that presumes that behaviours do not change. The reality is that they will.

The UK has managed to secure a deal. Japan, South Korea and India are mentioned as also possible deals in the near term.

They may be able to strike deals but the nature of those deals is difficult to predict. Reducing bilateral trade deficits will require countries to purchase more US goods but that will not be easy to do.

Much of the gripes from Trump are about foreign countries not buying US agricultural products. But there is no easy fix for that.

All this creates massive uncertainty and could have implications for inflationary expectations and geopolitical risks. Tariffs are a lose-lose policy and we have had plenty of evidence of that in the last few weeks. We suspect that surplus countries will be under pressure to allow their currencies to appreciate against the US dollar and there is some evidence the market is already beginning to price that (see page 16).

#### US imports average effective tariff %, 1790 – 2025 est.



Source: The Budget Lab at Yale, Waverton. As at 15.05.25

## 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 was extraordinary. Partly this is because of the media savvy of its leader, Elon Musk.

But that has changed in the last month with Musk taking a back seat, Trump deleting him from the Truth Social media site that Trump uses. We are moving on from DOGE.

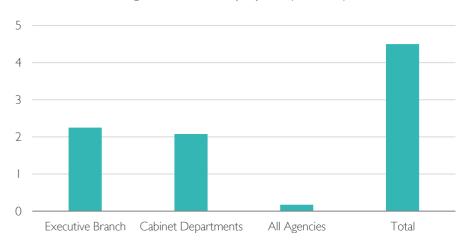
This makes a lot more sense than thinking DOGE could be effective. The Federal government spent \$7.1 trillion in 2024 according to the National Accounts. That is \$7.100 billion.

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 DOGE fired all of them, that would reduce government spending by just 6%.

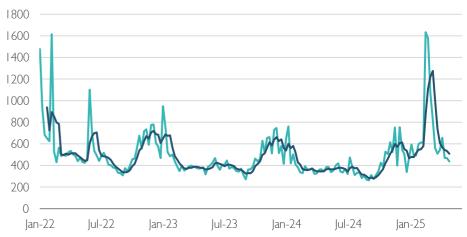
DOGE claims so far to have saved \$170bn but it is difficult to know how accurate that figure is. One piece of hard data that is useful is looking at initial unemployment claims of Federal Employees (the bottom chart). It ticked up in February but has since come back down.

We suspect DOGE can be taken out of the next edition of the Global Outlook.

#### Number of federal government employees (millions)



#### Initial Unemployment Insurance Claims by Federal Employees



Source: www.doge.gov, Department of Labor. Waverton. As at 02.05.25

## 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).

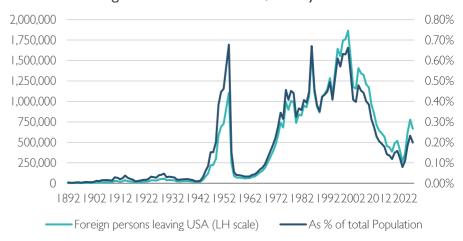
Trump is starting at a low base relative to history so may well be that he increases the number. But more people left by this measure in the Biden administration (2.0 million) than did in Trump 1.0 (1.8 million).

We can track the number of people removed (the last data is November 2024) so we can watch this closely. 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. Estimates vary, but the range is 25% - 50% of the workers in those industries are undocumented. Around 8 million work in construction and 2 million work in agriculture so 2.5 to 5.0 million of them are undocumented. The total US labour force is 164 million.

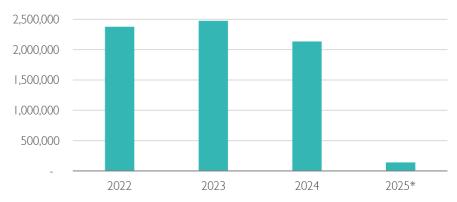
Trump does appear to be making migrants think twice about crossing the border. The bottom chart shows the number of people encountered at the south-west border by US Customs & Border Protection officers. In the last three months, a cumulative 34,762 have been encountered. That is 139,000 at an annualised basis. That is a reduction of 94% in the number of encounters compared to each of the three prior fiscal years.

We can infer from this that the number of people getting across without being encountered will be down dramatically too. If this continues, this will mean a meaningful reduction in the supply of cheap labour for the agricultural and construction industries. That could have an impact on wages in those industries. One to be watched closely in coming months.

#### Inadmissible foreigners who left the USA, fiscal years 1892 - 2025



#### Southwest Land Border Encounters, fiscal years 2022 – 2025



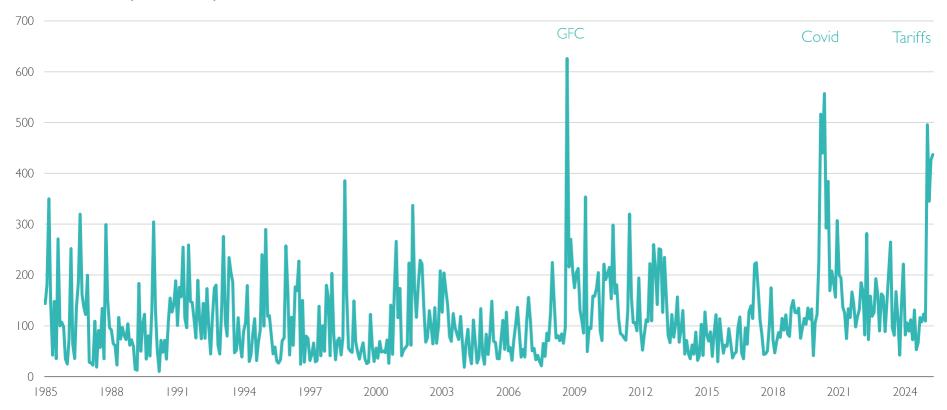
Source: <a href="https://www.cbp.gov/newsroom/stats/southwest-land-border-encounters">https://www.cbp.gov/newsroom/stats/southwest-land-border-encounters</a> and <a href="https://ohss.dhs.gov/topics/immigration/immigration-enforcement/immigration-enforcement-and-legal-processes-monthly">https://ohss.dhs.gov/topics/immigration/immigration-enforcement/immigration-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

\* data annualised from February, March, April 2025. As at 30.04.25

## ALL ADDS UP TO HIGH LEVELS OF UNCERTAINTY

The level of uncertainty surrounding US policy making is very high today. This index is calculated based on scanning thousands of press articles for those that cover "uncertainty" or "uncertain". A simple but effective way of thinking about periods of elevated confusion. One suspects the current situation is more in the category of "chaos" than uncertainty but we do not have a "Chaos" index.

#### US Economic Policy Uncertainty Index



**Source:** Baker, Bloom & Davis, Waverton. Data as at 30 April 2025.

## FISCAL POLICY WILL BE DOMINANT ISSUE IN 2025

This chart shows the US budget deficit as a % of US GDP. It is currently 6.8%. The deficit could become a bigger issue in coming months 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.

The bond market swooned in April and again in May. April appears to have been driven more by technical issues relating to the spread between yields on cash bonds and futures. But May has seen the bond vigilantes putting their heads above the parapet. That could be a challenge in the months ahead.

#### US budget balance as % of GDP 1970 - current



**Source:** Bloomberg, Waverton. As at 30.04.25

## RATE CUTS STILL 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 April 1st, the day before the tariff announcements.

The market thinks the Federal Reserve will cut rates two or three times by the end of the year. For that to happen, growth will have to slow materially in the months ahead and expectations for inflation will need to remain well anchored.

In the UK expectations have not really changed in the last few weeks (and the teal line in the below chart is after the higher than expected inflation report for April). The market is expecting one rate cut by the end of the year.

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, Waverton. As at 21.05.25

#### TREASURIES SELL-OFF

The top chart shows how the yield on 10-year gilts and 10-year US Treasuries has evolved over the last two years.

US Treasuries had rallied in March but have given that back since just after the Liberation Day tariff announcement. Consequently the gap between Treasury and gilt yields has narrowed and is back to a more "normal" spread.

The problem for Treasuries is in part that there are no signs that the budget deficit is going to do anything other than expand from its current 6.8% of GDP.

The bottom chart shows those same yields after deducting the current IO-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).

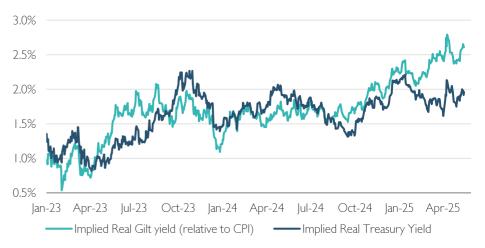
As the chart shows, both markets continue to offer, on this measure, a positive real yield. The inflation linked bond market is saying something similar in the US where the Treasury Inflation Protected Securities market is giving a positive real yield. The January 2035 TIPS yields 2.1%. The UK linker market is optically less attractive (the September 2035 linker yields 1.5%) 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, Waverton. As at 19.05.25

## INFLATION RATES HAVE DECELERATED AROUND THE WORLD

The peak for US inflation was in June 2022 at 9.1%. It is now 2.3%. The euro area peaked in October 2022 at 10.6% (now 2.2%) and the UK also peaked in October 2022 when RPI was 14.2%, and CPI 11.1%. RPI is now 4.5% and CPI is 3.5%.

US core inflation (excluding food and energy) peaked at 6.6% in September 2022. It is now 2.8%.

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)



Source: Bloomberg, Waverton. As at 21.05.25

## EXPECTATIONS FOR FUTURE INFLATION REMAIN ANCHORED

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 continues to have anchored expectations for inflation over the next five years. But we need to watch this closely as the recent uptick in the US (teal line in top chart) is of concern.

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

The teal line is the 10-year US inflation swap and the dark grey 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.

One of the critical things to watch in coming weeks will be to see if the finalisation of tariff levels does anything to these measures of expected inflation.

#### 5-year inflation swap rate (%)



#### Long-term US inflation expectations



Source: Bloomberg, Waverton. As at 21.05.25

## THE BROAD COMMODITY COMPLEX HAS BEEN WEAK

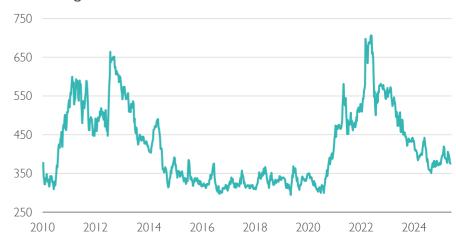
The broad commodity complex is in the doldrums.

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. Meanwhile the imposition of significant US tariffs could further pressure the economy in a negative way.

#### S&P GSCI grains index



#### S&P GSCI industrial metals index



Source: Waverton, Bloomberg. As at 11.04.25

#### DOLLAR WEAK THIS YEAR

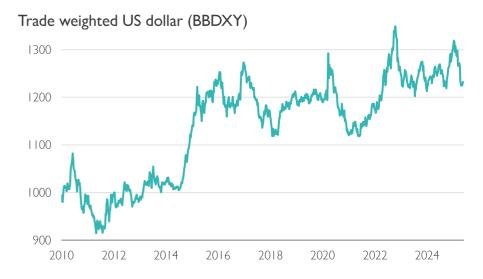
The top chart shows a trade weighted dollar index. It has been weakening this year and has been particularly weak since the 2 April tariff announcements.

Some of that is possibly due to the market expecting there to be pressure on countries with a trade surplus to allow a strengthening of their currencies against the dollar.

Some of it may reflect some generic nervousness about US dollar assets, although such a thing is very difficult to model with any confidence.

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 US dollar is up against EM currencies this year and has risen materially since mid-April. This could certainly be tariff related. It is also interesting that the dollar has not been appreciating meaningfully against the Renminbi which is the largest component of the EM currency index in the bottom chart.



#### MSCI emerging market currency index



Source: Waverton, Bloomberg, MSCI. As at 19.05.25

## STERLING STILL RANGEBOUND AGAINST THE EURO, BUT WEAKER OF LATE

Sterling has strengthened against the euro in May. The dip in sterling against the euro in early April in the wake of the initial shock at the extent and size of the tariffs announced by President Trump, was rather surprising given that for a lot of European manufacturing companies the tariffs are going to be a serious headwind.

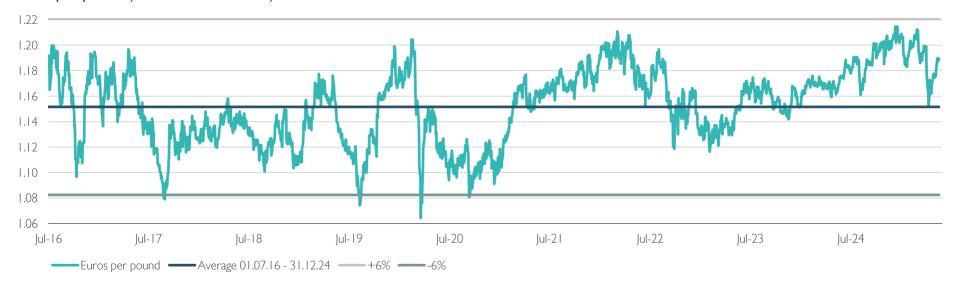
As for the UK, we continue to think that the exchange rate versus the euro is a better measure of the market view of UK specific risks than the sterling/dollar rate. The chart shows the number of euros per pound since I July 2016. The average exchange rate since then is shown as the blue line and we 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.

#### Euros per pound (01.07.2016 – current)



Source: Bloomberg, Waverton. As at 19.05.25

## GOLD AT A RECORD HIGH

As of the end of April 2025, gold was 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 \$3,123. The value of the gold held by the US government is \$11bn at the \$42 valuation. It would be over \$800 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



Source: Bloomberg, Waverton. As at 30.04.25



## 2025 EARNINGS GROWTH ESTIMATE + 11% GLOBALLY AND +9% FOR THE US

For 2025 the consensus numbers have come down quite a lot in the last month.

US has gone from +14% to +9%.

World has gone from +13% to +11%.

This is not surprising given that despite the strong earnings reported in Q1 the nervousness about the impact of tariffs creates uncertainty across the corporate world, not just in the US.

The bounce back in 2026 to +13% and +14% suggests analysts, likely guided by companies, are not expecting a persistent negative effect. Let's see if that is too optimistic.

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

			GROWTH RATE		
REGION	PE NTM	RELATIVE	2025	2026	2027
World	17.2		+10.7%	+12.6%	+10.9%
US	20.4	119%	+9.3%	+13.7%	+12.5%
Europe ex UK	14.5	84%	+12.8%	+12.7%	+10.5%
UK	12.0	70%	+4.5%	+12.0%	+9.5%
Japan	13.6	79%	+13.5%	+8.7%	+6.5%
Asia Pac ex Japan	12.6	73%	+13.7%	+12.2%	+12.3%
Latin America	8.8	51%	+39.4%	+9.3%	+11.5%
Emerging markets	13.6	80%	+14.6%	+11.9%	+10.8%
World ex USA	13.4	78%	+12.4%	+11.4%	+9.3%

Source: MSCI, FactSet, Waverton. Data as at 30.04.25

## STOCK MARKET VALUATION LOWER

The PE ratio for the US market (solid teal line) is 20.4 times (as at the end of April).

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

The World outside the US now trades at 13.4 times earnings, a little above its 20-year average of 13.1.

There is always uncertainty about the EPS these valuations are predicated on, and even greater uncertainty at the moment. But particularly outside the US there is a reasonable amount of uncertainty priced in suggesting that on any good news global markets could well rally strongly.

#### MSCI US and MSCI Global ex US price-earnings ratio based on next 12 months earnings



Source: MSCI, FactSet, Waverton, As at 30.04.25

## 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 (teal line) and the PE of an equally weighted version of the S&P500 index, both on forward earnings.

The former is at 23 times, the latter is at 18 times (as of May 15<sup>th</sup>). The discount has widened out again having narrowed with the market

correction in early April.

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, even before the correction.

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.

#### S&P500 Index and S&P500 Equal Weighted Index, price earnings ratio 2010 - current



Source: Factset, Waverton, As at 15.05.25

# US PROFITS AS % OF GDP AT RECORD HIGH IN Q4 2024

This chart shows pre-tax profits of corporate America relative to GDP through Q4 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 at a record high of 13.5% of GDP. This is another indicator suggesting a recession in the near term is unlikely, and indeed confirms that the

health of the corporate sector is genuinely robust.

However, the tariff policy will be a hit to profits in some sectors of the economy. Indeed, if anything, it is likely to be a bigger problem for small and medium size businesses than it is for the giant multinationals. A company like Apple has been given favourable treatment by having tariffs on phones and other products being exempted from extra tariffs.

So although at the moment this is an indicator suggesting the corporate sector is in good health that could change quite quickly.

#### US profit cycles and recessions (%)



Source: MSCI, FactSet, Waverton, As at 31,12,24

## 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, Waverton. As at 16.05.25

# 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 2024 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, only ending negative policy rates in March 2024. The policy rate is now at +0.5% having been raised again in January 2025. 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.

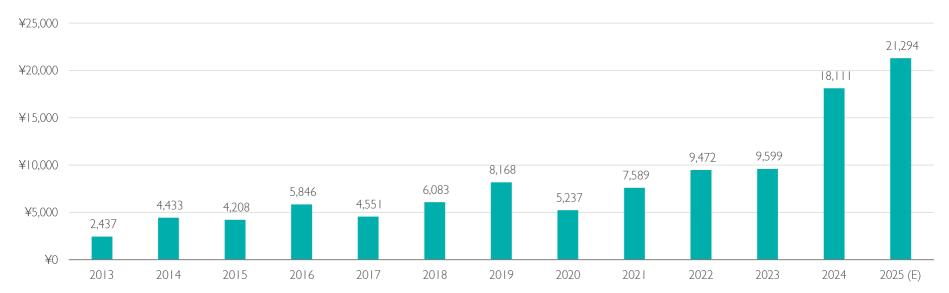
Shareholders have benefitted directly from a significant pick-up in the number of buybacks done by Japanese corporates.

This chart shows that buybacks were at a record level in 2024, 89% above the level of 2023. They are expected, according to Mizuho, to rise another 18% in 2025 to 21.3 billion yen, or \$146 billion at the current exchange rate.

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 billions of Japanese yen



**Source:** Mizuho, Tokyo Stock Exchange. As at 03.04.25

#### US INVESTOR SENTIMENT BEARISH

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 (dark blue line) the average level and one standard deviation below (grey line).

If you buy the market when the teal line is below the grey line your

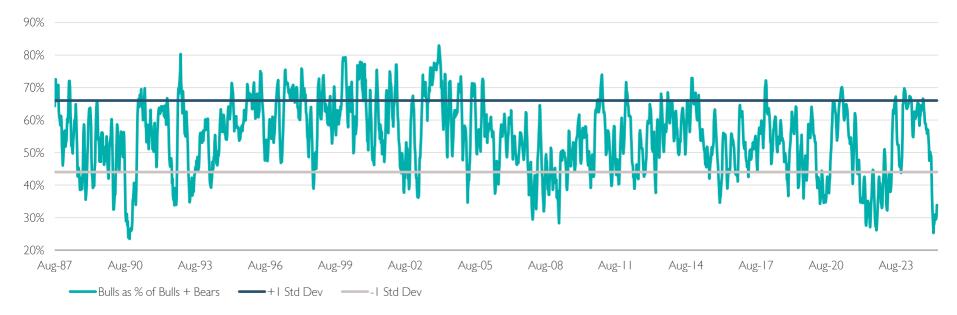
average return in the next year is +15%.

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

This sentiment measure followed the market down in March and April but it has remained depressed despite the bounce of the early April lows.

One of the bits of good news for the market is that by this measure at least, investors are already very bearish.

#### American Association of Individual Investors survey, Bulls as % of Bulls plus Bears



Source: AAII, Bloomberg, Waverton. As at 15.05.25

## 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 Q3 and Q4 2024, and in O1 2025.

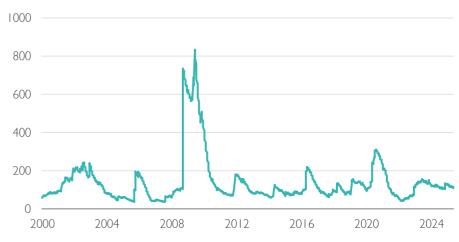
The Bloomberg Index in the bottom chart is of economy wide US bankruptcies and takes into account the size of the bankruptcy as well as the number of them. Hence there were more big bankruptcies in 2009-10 than in 2003-04. That index is at historically very low levels.

It remains the case that up to now, corporate balance sheets are holding up well. There has to be a risk that widespread tariffs change this benign picture.

#### US bankruptcy filings (2000 to current, quarterly)



#### Bloomberg US Corporate Bankruptcy Index (2000 – current, weekly)



Source: Bloomberg, Waverton. As at 16.05.25

## CORPORATE CREDIT MARKETS COME OFF THE BOIL

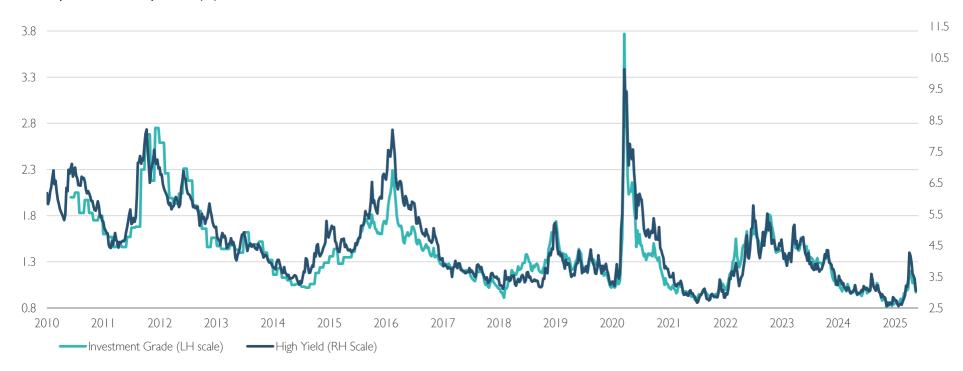
Credit spreads widened in the wake of the tariff announcements on 2 April. But they have quickly narrowed again as markets rallied.

Spreads will widen again if there is a risk of slower growth and higher inflation.

We remain of the view that credit spreads have further to widen to better reflect the risks.

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

#### US corporate bond spreads (%)



**Source:** Markit, Bloomberg Waverton. As at 16.05.25

## 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 April 2025, the numbers were 6.2% versus 5.0%.

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 and

2024 both gave good returns.

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 Waverton. As at 30.04.25

# WEAKNESS OF CHINESE CURRENCY NEEDS TO BE WATCHED

The Rmb has been weak since the US Presidential election in early November. The uncertainty of the US tariffs are not helping matters.

The sluggishness of the Chinese economy is also an issue with retail sales and industrial production being the latest datapoints to reflect that.

There has been a big appreciation of the Taiwanese dollar in recent weeks. It ended March at 33.2 to the US dollar and is now at 30.2 so it has appreciated by about 10% against the US dollar.

A number of factors seem to be at play. One is that there is speculation that the US will want currency appreciation of surplus countries against the US dollar. The Taiwanese central bank did not intervene when the Taiwan dollar appreciated particularly sharply May 2<sup>nd</sup> and May 5<sup>th</sup> which also led to speculation along the same lines. The TWD is normally a heavily managed floating currency which the Central bank has regularly intervened to impact trading.

As we saw on page 16, the global emerging market country currency index has been strong against the US dollar since January 2025. We suspect this reflects the presumption that EM countries that have trade surpluses with the US will be expected to allow their currencies to appreciate.

# Renminbi per US dollar



#### Taiwan dollar per US dollar



Source: Bloomberg, Waverton. As at 16.05.25

Part 3 OUR APPROACH TO INVESTING RESPONSIBLY

#### OVERVIEW OF RESPONSIBLE INVESTMENT AT WAVERTON

Signatory of:













#### 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



## **Engagement and voting**

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

#### **Ethical restrictions**

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

#### 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 focussed 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:













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