Investment Commentaries

Market Forces and Policy Reality: What Must Happen Will and What Can't Happen Won't

Markets have an inherent ability to separate facts from fiction. The process of capital allocation imposes accountability on politics and ultimately determines which policies can be sustained and which cannot. Bond markets constrain excessive government spending through higher borrowing costs. Currency markets discipline protectionist trade policies through devaluation, worsening import price inflation. Equity markets direct capital toward projects with genuine economic returns rather than political appeal. This market discipline provides the basis for economic growth and prosperity.

This fundamental truth - that what must happen will and what can't happen won't - provides an important perspective amid the geopolitical and macro-economic uncertainty.

We began 2025 with a constructive outlook based on strong economic fundamentals: robust corporate investment in efficiency, capacity and innovation; resilient consumer spending supported by rising real wages; moderating inflation and supportive monetary policy. The Trump administration's deliberately disruptive approach to domestic and foreign policy has increased uncertainty and market volatility, creating both opportunities and challenges for companies, consumers and investors.

However, volatility can be positive as well as negative, and as the strong performance of our World Stars Global Equity strategy this year has shown so far, it has been right to take a long-term and reasoned view that the US government's policies, whether on tariffs and trade restrictions, cost cutting, spending or immigration would differ from their announcements and that they would be constrained by the reality of US economic needs and global financial markets.

While political and economic uncertainty has increased, our investment approach remains focused on underlying business fundamentals. Company earnings, management meetings, and our research and recent travel across the US and Europe show that they remain resilient. The US economy in particular has compelling long-term growth drivers: investment in computing capacity, data centres and AI to drive efficiencies and growth; necessary infrastructure investment to close the productivity gap; and the continued financial strength of many consumers. Businesses and consumers are clearly affected by the uncertainty and if it should lead to economic slowdown, higher inflation or other issues, it is possible if not likely that market constraints and political considerations will lead to changes in government policies as they have already.

Our investment approach remains consistent: focus on quality companies, maintain valuation discipline, and take advantage of opportunities created by market volatility.

We invest in high-quality companies with strong competitive positions; the ability to grow through innovation, capital allocation or growing markets; led by experienced management teams with proven track records of creating shareholder value; and supported by robust balance sheets that can weather economic adversity. These quality attributes position our companies not just to survive periods of uncertainty but enables them to act rather than having to react. They can allocate capital to reinvestment, acquisitions or return to shareholders, and can make use of adversity to get stronger and to increase their scope for value creation. At the same time our focus on valuation means that we ourselves can act to reallocate capital from companies whose valuations are higher or whose prospects for growth and value creation are lower to new positions or to reinforcing existing ones.

This consistency explains the resilient performance of our World Stars Global Equity strategy, which has returned close to its previous highs. Our experience has been that quality companies bought at reasonable prices outperform when markets focus on fundamentals rather than sentiment. This approach has served us well through previous periods of uncertainty and crisis, and as this year has shown, our companies are positioned to benefit from the quality of their businesses and the underlying economic resilience while providing protection against policy-driven volatility.

The principle that what must happen will and what can't happen won't provides both clarity and confidence in focusing on facts and fundamentals. Markets will continue to hold governments accountable, creating opportunities for long-term investors who are able to act with consistency and discipline while others react to headlines. We remain optimistic about the long-term prospects for our quality companies and will look to take advantage of opportunities as they arise.

World Stars Global Equity webinar, Tuesday 15th July, 14.30 UK time

Please join us for an update on our performance and our views on the outlook for companies and markets in 2025. You can register using the link below:

https://us02web.zoom.us/webinar/register/WN_tPmLa3TdQpyh-U_WaoCwVw

World Stars Global Equity

Our World Stars Global Equity strategy was up 6.1% in US dollar terms in May, driven by strong fundamental earnings reports, supportive valuations and signs of flexibility in US government negotiations with trading partners. The strong performance means the strategy is now up +3.4% year to date, broadly in line with global indices. You can find our latest factsheet here.

Media and entertainment leader Walt Disney was up 24% as the company reported further improvement in the profitability of its streaming business. At the same time its parks business continued its resilient performance, with strong bookings and decisions to expand its California and Florida parks to accommodate the strong demand.

Semiconductor leader Nvidia was also up 24%. The company reported another record quarter with USD 44 billion in revenues, comfortably beating market expectations. Management said it expected further acceleration in the next quarter, raising revenue guidance to USD 45 billion despite the recent US government restrictions on the sale of its products to China. As use cases for AI solutions multiply and significant investments by sovereign governments add to the demand for computing capacity, Nvidia is in a powerful position to take advantage of this growth.

Meta, the social media platform, was up 18% in May and once again evidenced the business case for AI, with strong results driven by tangible AI-driven improvements in targeting, engagement, and ad performance.

Increased demand for AI investments also benefitted some of our industrial holdings including electronic connector leader Amphenol and power management company Eaton. Other industrial holdings continued to benefit from strong demand in aerospace and defence, with RTX and Honeywell both up 8%.

On the weaker side during the month was Alcon, the ophthalmology leader, down -11%. The company faced short-term headwinds from a soft US surgical market and customers holding back certain equipment purchases in anticipation of a new product launch in May. We believe that these issues are transient and that the company remains exceptionally well positioned in a highly attractive niche within the healthcare industry. New product introductions in surgical equipment and implantable lenses should help to drive growth in the quarters ahead.

Multi-Asset Income

As global market sentiment continued to improve last month, our Multi-Asset Income strategy showed a positive return of 1.6% (now up 1.9% year to date). Equities were the main contributor, followed by our investment funds and fixed income.

Eli Lilly was again a volatile feature in May (-18%). Following a strong performance in April it suffered from the poor performance of its main competitor Novo Nordisk and comments about product prices coming down faster than anticipated.

Our fixed income portfolio suffered somewhat from the rise in term premium as investors refocused their attention on the rapid growth of the US public debt.

Our funds portfolio is still seeing interest from investors looking for value in expectation of interest rates being cut by the UK central bank.

Tariff noise and the resulting macroeconomic uncertainty have subsided, only to be replaced by President Trump's "Big Beautiful Bill" with prospects of a much greater budget deficit and lack of clarity around 'revenge taxes'. So far, the US economy has been remarkably resilient, supporting the US equity market, which seems to ignore the possibility of slower growth. However, fixed income and currency markets are clearly concerned by the rising US budget deficit and yields are adjusting to the prospect of government debt supply later this year. In this context we expect volatility to remain a main feature of risk assets over the summer months.

In line with the investment mandate of our Multi-Asset Income strategy, our defensive positioning has paid dividends year to date and we are confident that the high visibility provided by our emerging market corporate debt exposure will stabilize our portfolio for the rest of the year.

Current economic data, which mostly predate 'Liberation Day' tariff announcements, still provide a constructive picture of the US economy. How this picture may change over the near future will be key to the outlook for risk assets for the rest of the year.

The chairman of the Federal Reserve has confirmed that in their view the uncertainty around unemployment and inflation have risen and as a result their future decision will be driven by future economic data releases with no reason to rush now, which is somewhat at odds with the markets' expectations for 4 to 5 interest rate cuts. In our view this opens the door to further bouts of elevated volatility over the next six months.

We remain positioned to navigate this sort of environment with our emerging market bonds exposure which provides great visibility with a yield to maturity of around 8.8% for the next 2.7 years and also lower relative volatility.

Emerging Market Debt

Our Emerging Market Bond strategy was up 0.9% for the month and up 2.1% year-to-date, both in US dollar terms. You can find our latest factsheet here.

Risk assets rebounded on the back of a US-China trade truce and EU tariffs put on hold. At the same time, US treasury yields widened on concerns over the US fiscal deficit. The combination led to emerging market credit spreads tightening marginally over the month.

The earnings season continued to highlight the strength of underlying corporates. Total Play (Mexico; communication) saw good subscriber growth as it focused on increasing penetration rates from its existing network. This translated to better free cash flow and liquidity with management reiterating their focus on further improving the capital structure.

Corporates in the commodity sector exercised discipline on capital allocation. YPF (Argentina; energy) reported a 50% increase in EBITDA, supported by cost savings from divestment of non-core assets. The company continued with its transition from conventional to shale and a focus on growing its export volumes. Sibanye Stillwater (South Africa; mining) also reported a 90% improvement in EBITDA helped by corporate restructuring efforts and the surge in gold prices. Lastly, Tullow Oil (Ghana; energy) agreed the sale of assets in Gabon with proceeds used to reduce net debt and refinancing risk.

US policy will continue to drive risk sentiment. Frequent changes in policy have led to a period of high uncertainty which is likely to keep volatility elevated. We have and will continue to take advantage of this, adding to compelling opportunities where valuations deviate from strong underlying credit fundamentals. Our focus is on relatively short duration bonds with good income yield which provide visibility on returns and downside protection.

Today, our Emerging Market Bond strategy offers an 8.8% per annum yield to maturity (in US dollar terms) with a relatively short duration of 2.7 years. This comprises a 7.9% per annum income yield which provides a degree of visibility on future returns as well as capital appreciation potential given the average bond price is 97 cents on the dollar.

June 2025