2025 INVESTMENT OUTLOOK

As markets come to terms with Donald Trump's second term, I take a look at the investment outlook for 2025.

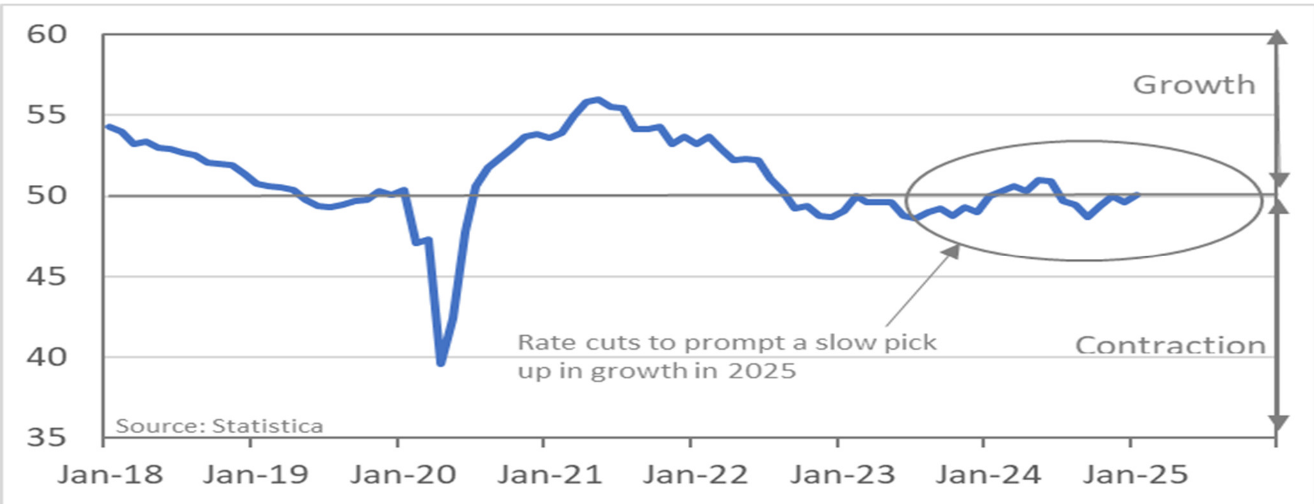
Will Donald Trump impose widespread tariffs on US imports?

Markets were shocked when Donald Trump suddenly announced 25 percent tariffs on Mexico and Canada. However, within seventy-two hours, after concessions had been extracted from both countries, the implementation of tariffs was postponed for another month to allow further negotiation. This episode tends to suggest that Trump views the threat of tariffs, around the world's largest economy, as a means of furthering American commercial interests rather than a long-term economic policy. If Trump had been serious about implementing a meaningful tariff policy, then he would have surely adopted the suggestion of his Treasury secretary by starting with a small tariff and gradually increasing it over time. This approach would have minimised the disruption to commerce. Suddenly imposing 25% tariffs, in a region that had benefited from free trade since 1994, would have caused significant economic dislocation. So, if countries are prepared to offer Trump concessions it seems that the worst of a trade war could be avoided. As Trump recently remarked 'Tariffs are very powerful, both economically and in getting everything else you want. When you are the pot of gold, the tariffs are very good.'

What is the cyclical outlook for the global economy?

The cyclical outlook for the global economy is obviously greatly influenced by the magnitude of tariffs imposed by Trump and any associated retaliation. On the assumption that deals can be done to limit the extent of any tariff increases then the outlook is for a slow and gradual recovery. Following the normalisation of inflation central banks have started to cut interest rates. However, with inflation still above target in the UK and the US both the Bank of England and the Federal Reserve are cautious about large interest rate cuts. The Eurozone is the only region where the central bank feels it has the

CHART 1: THE OUTLOOK FOR GLOBAL MANUFACTURING



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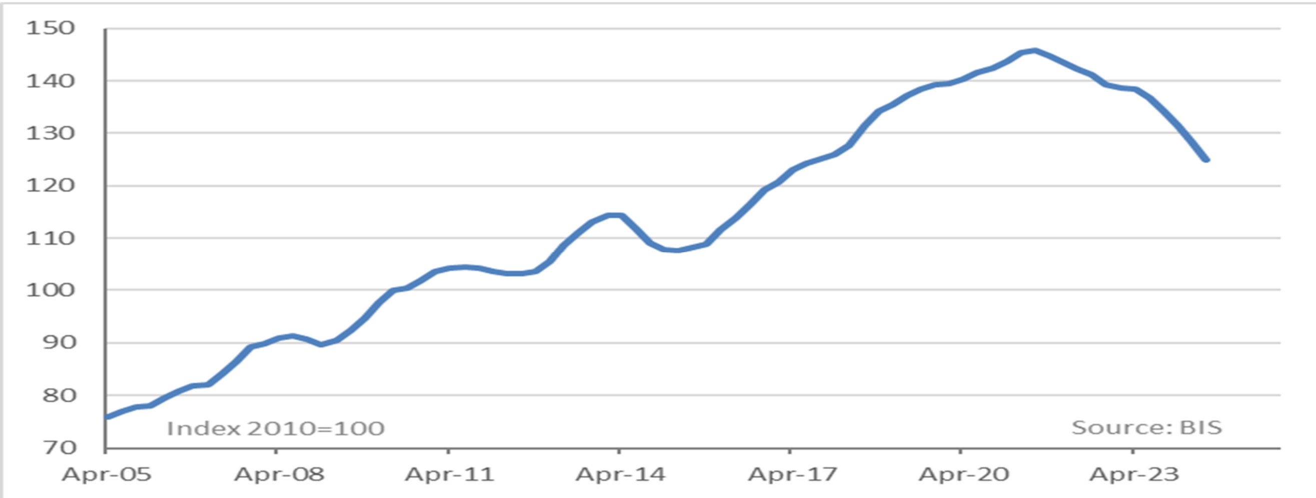
scope to aggressively cut interest rates. The global economy will also benefit from the end of post pandemic destocking (when the pandemic was at its height companies boosted stocks due to uncertainty about supply, subsequently when the pandemic ended, and as supply became more predictable, these stocks were run down.) However, with the Chinese economy still struggling what is less clear is where the positive demand shock will come from to drive a meaningful acceleration in growth.

Is there an end in sight to the downturn in the Chinese economy?

The Chinese economy continues to struggle under the weight of a property market downturn that began in 2022. Housing is economically important as about 70% of consumer wealth is invested in property. This means it is a key determinant of business and consumer confidence. Whilst the property market has probably passed its worst house prices continue to fall. So, a meaningful rebound in the Chinese economy is unlikely this year. In recent decades property construction has been a key motor of the economy. However, with the Chinese population now falling China needs to find a new growth model. The most obvious solution would be to encourage Chinese consumers to save less (China's saving rate is around 40% compared to the UK's 10%) and spend more. Practical measures to promote this would be bullish for both the Chinese and Asian economies.

CHART 2: CHINESE HOUSE PRICES ARE STILL FALLING



What is the outlook for technology shares and Artificial Intelligence?

Enthusiasm for Artificial Intelligence (AI) has been the driving force behind stock markets for the last two years. In 2025 the big four US technology companies expect to spend USD 320 bn on building out AI up from USD 230 bn in 2024. Investors had assumed that US technology companies would have a dominant position in AI and that there was a strong link between money spent and capability in AI. However, the new AI models produced by the Chinese company DeepSeek call both of these assumptions into question. Not only are they on a par with the best models of the American tech companies but they were developed much more cheaply and use significantly less computing power. This has triggered a modest correction in the shares of US technology companies. With investors now much more focused on the revenue generated from these huge investments the risk is that valuations correct further.

Conclusion

I have argued that Trump's tariff threats are largely a negotiating tool rather than a desire for the United States to become more self-sufficient and less integrated into the global economy. On this basis the global economy is likely to achieve modest growth as it slowly recovers from destocking, the shock of higher interest rates and the Chinese property downturn. As a result, the outlook for the majority of UK multi-nationals is reasonably constructive. However, some volatility is to be expected as markets wrestle with how to price the Artificial Intelligence opportunity for the dominant US tech companies.

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