

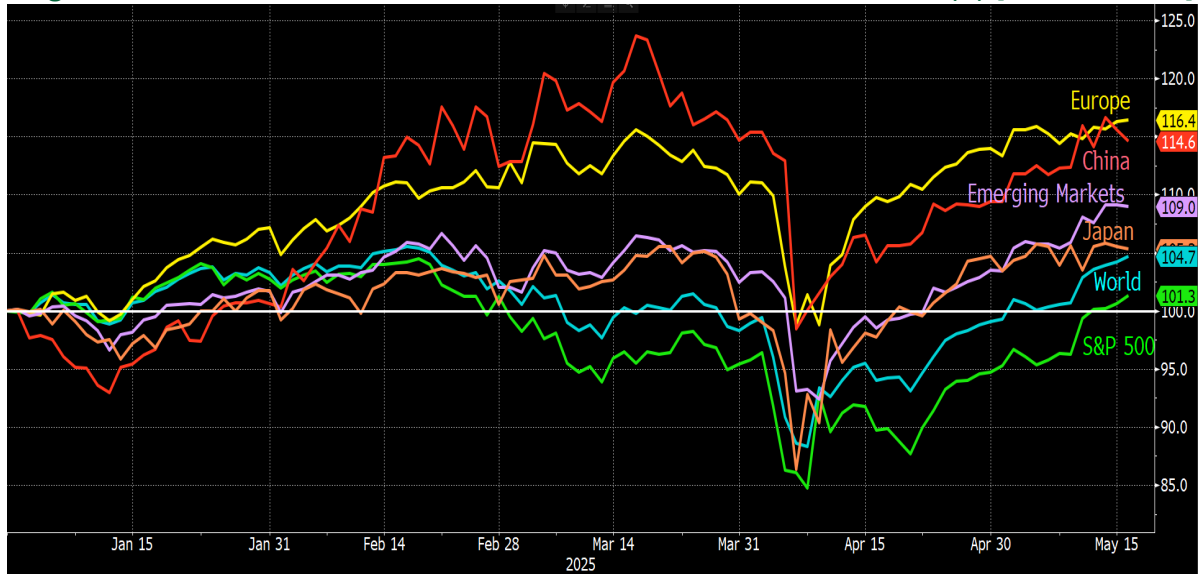
*"Facts are stubborn things."*

*Ronald Reagan*

## 1. AFTERALL

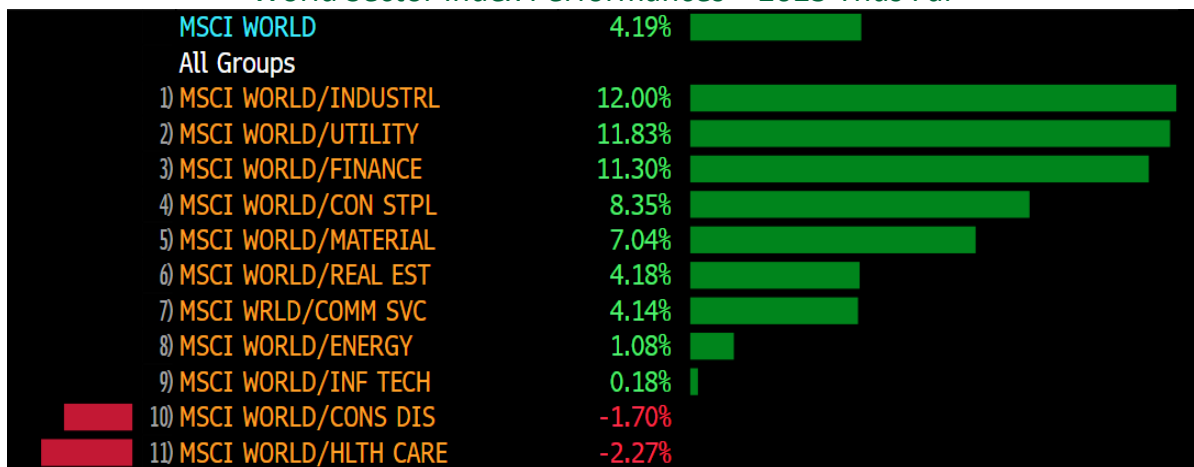
The capital market volatility following the *Liberation Day* announcements on 2 April reached similar levels to those experienced during the Credit Crisis and the Pandemic. Whilst the tariffs are expected to impact world trade and economic growth, we formed the opinion that the impact would not be as severe and therefore investors should be careful not to overreact. The following chart reflects stock market performances this year thus far:

Regional Stock Market Performances – Indexed to End 2024 = 100 (\$) [MSCI Indices]



All the major regions have recovered their losses, with Europe, China and Emerging Markets doing particularly well, at the cost of the US (S&P 500). The flight of capital from the US clearly reflects in these performances.

World Sector Index Performances – 2025 Thus Far

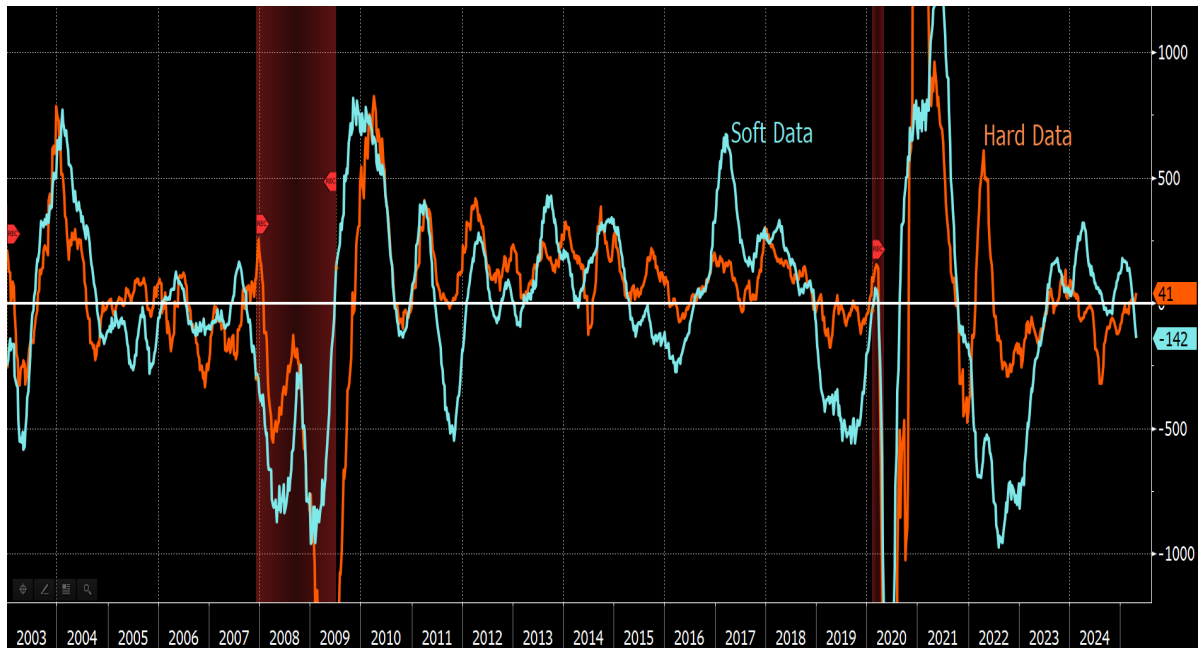


The best performing sectors, in sequence, have been Industrials, Utilities, Finance and Consumer Staples, generally the more defensive sectors. Healthcare, Consumer Discretionary and Information Technology did the worst. Technology suffered from the capital flight out of the US. This rotation may offer opportunities worth exploring.

## 2. US ECONOMY

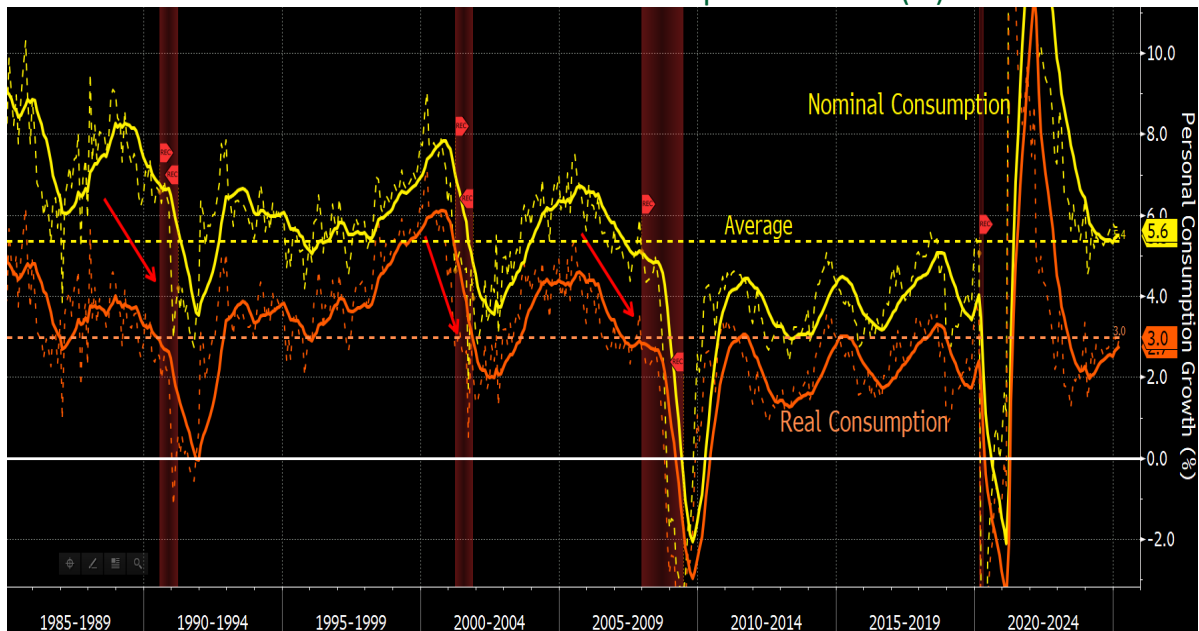
Investors currently face a major conundrum as, logically, tariffs are going to affect the economy, with little certainty to what extent. Thus far, the economy remains resilient.

US – Citi Hard vs Soft Economic Data



The Hard Economic Data Index of real economic activity is in the process of recovering and is currently in positive territory. Against this, the Soft Data Index (considering the outlook) is dropping and currently in negative territory. This discrepancy may continue for a while still, leaving investors uncertain.

US – Nominal and Real Consumption Growth (%)



Critically, US consumption remains well on track, in both nominal and real terms, and both series growing on their respective long-term average levels. The major uncertainty is whether tariffs are going to materially affect these economic support factors. On the supportive side, new employment and wage growth remain resilient at historic average levels, and above general expectations.

Economic backlogs are in the process of becoming less supportive. Tariffs are already causing unnatural economic activity and may affect Hard Data. Investors have no choice but to closely follow developments and be alert when Hard Data may have higher risk of reversing its current course.



### 3. INVESTOR SENTIMENT

It is striking how quickly stock markets recovered following President Trump’s announcement of the 90-day tariff negotiation period. We believe this recovery is also based on negotiation results being constructive thus far. The following charts reflect this recovery in investor sentiment:

US – High Yield Corporate Bond Spread (%)



Whilst remaining to be relatively low, the above Corporate Bond Spread has recently reversed its short spike. This indicates a recovery in investor sentiment, expressing a view that there is no material risk in continuing to get their corporate bond income from smaller, more risky type of corporates.

US – Nominal S&P 500 Equity Risk Premium – ERP (%)



The above ERP Index reflects the difference between the Earnings Yield and the Treasury Yield and indicates investors’ confidence that Equities will outperform Bonds. The lower the charts’ level, the higher the confidence.

Investors took a positive stance before *Liberation Day* but quickly reversed course from 2 April with the ERP spiking into positive value. This has recently reversed, with the ERP again in negative territory. This reflects renewed strong investor sentiment.

Whilst these conclusions are constructive, it also highlights the valuation risks should the end tariff results become disruptive and affect economic and earnings growth. We guard against complacency on Equity valuations.



## 4. EUROPE

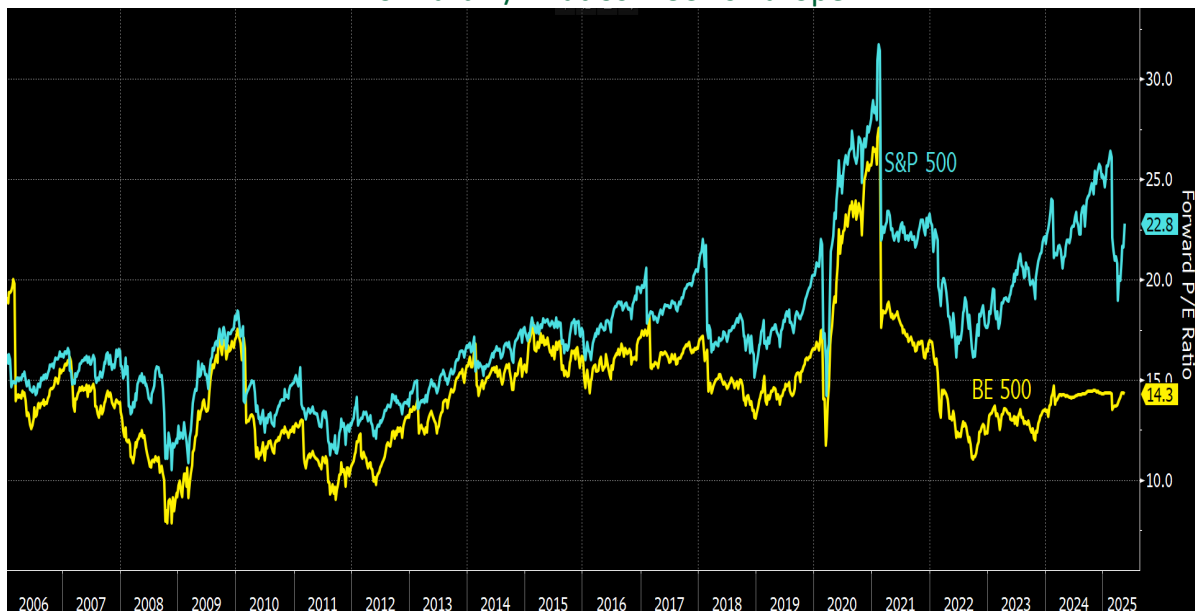
Europe has become an increasingly attractive investor destination for two main reasons, being the flight of capital from the US and the material change in its leaders' willingness to increase their defense budgets. Investors must consider to what extent this may lead to more structural changes on this front.

### Consumer Confidence Index – US vs Europe



The European Consumer Confidence Index struggled to recover after the Pandemic. It has not yet reached its long-term average level and started to drop again at the beginning of this year. Against this, the US's Index remained well above average, but the most recent reading also dropped sharply. In this context, it seems that the two regions are currently in the same proverbial boat.

### Forward P/E Ratios – US vs Europe



US businesses generally benefit from a more business-friendly regulatory environment (and further potential softening), better entrepreneurship, more investment opportunities and better returns on investment, higher economic growth and deeper capital markets. Stock market valuations, therefore, have been at a premium.

Index compositions and constituents differ materially between the two regions. All said, though, we believe investors are now more conscious of the valuation discrepancies in the above chart, with potential that European jewels may rerate quickly.



## 5. CHINA

Following *Liberation Day*, and after a long period of disinvestment, investors are now taking more notice of China as an investment destination. We consider to what extent Western comfort to invest in China may have recovered. The discount at which a China closed-end fund trades can be some indication:

Fidelity China Special Situations Fund – NAV vs Share Price (£p)



The ratio of the Net Asset Value (NAV) over the share price is currently 1.10 times (+10% upside). This is on the long-term average, and below the 2024 levels. With other Western market quality closed-end funds also at this level, this indicates that investor comfort is neutral in this context.

Tencent – Target Valuation vs Share Price (HK)



Tencent's chart in this context reflects a similar picture. Its current Valuation Upside of +25% is on its long-term average. This also reflects the market's neutral perception.

China is very exposed to US tariffs. The way in which they deal with this can be a major determinant as to whether foreign investors reconsider their withdrawal from the region.



## 6. MAGNIFICENT SEVEN

With the flight of capital from the US stock market, index selling has affected the Magnificent Seven stocks directly:

Magnificent Seven Forward P/E Relative to S&P 500



Their relative valuation currently is almost two Standard deviations below average. That is roughly at the same level when the aggressive Federal Reserve tightening affected them severely in 2022.

Amazon vs Walmart – Relative Price and Relative Forward P/E



Many investors prefer the staple nature of Walmart to the technology angle in Amazon, to the extent that Amazon's valuation is currently at a quarter discount to Walmart's (the orange line) – even though its growth outlook is double the latter's. The stock has severely underperformed Walmart (the yellow line), despite them having similar tariff implications and Amazon's strong cloud exposure. It seems this severe underperformance has recently turned the corner (highlighted).

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