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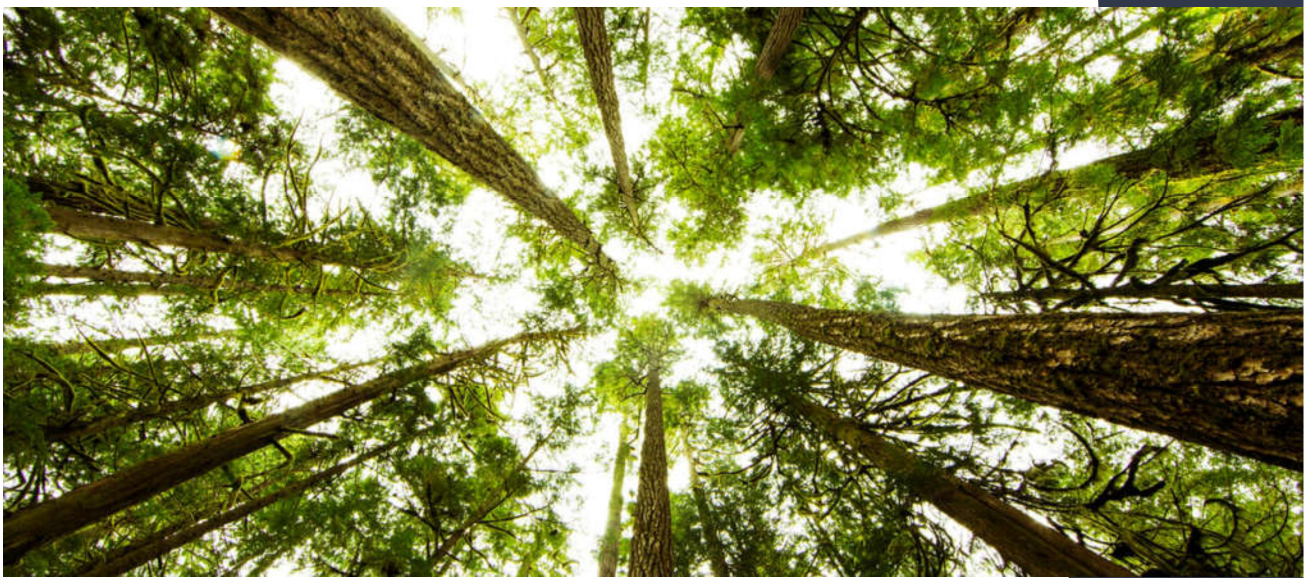
Hyperactivity



John Wyn-Evans
Head of Investment Strategy

Back in my childhood, there were quite a few of my fellow pupils who were deemed to be “naughty boys”. Had they been at school today, I suspect that the majority of them would have been diagnosed with ADHD or an associated hyperactivity disorder. Their educational journey would have been a lot more productive with the correct counselling and/or medication and they would have been far less disruptive to the rest of us (although I must admit I wasn’t perfectly behaved at all times!). At least the disruptions were largely confined to the classroom. It's a different issue when the "leader of the free world" displays disruptive tendencies. How are we, as investors, supposed to deal with that? Unfortunately, we can't just ignore them. Indeed, I now wake up on most mornings wondering "What has he done now?"

The consensus amongst the investment strategy community is that there are both good and bad elements to President Trump's policies. If you are an optimist (or a Republican), you might prefer to focus on the "bonfire of red tape" and drive to deregulate as well as on the potential for Elon Musk and his DOGE recruits to slash government spending. If you are a pessimist (or a Democrat), your concerns will be ignited by Trump's policies on, for example, trade, tariffs, and immigration, as well his cavalier attitude to geopolitical issues.

As we are generally "in the market" and thus well placed to ride a wave of good news, let's focus on the negatives. Do we need to position more cautiously or take evasive action? Our working opinion at the tactical asset allocation level is not, although we are by no means blasé. Indeed (so far, at least), it would have been a mistake to reduce risk on any news of tariffs being imposed. There has been either a swift resolution (or we could call that "backing down" in the case of Colombia) and a stay of execution for both Mexico and Canada. Yes, they had to announce concessions in terms of tightening up their borders, for example, but they were not too onerous. Admittedly, the initial tariffs on China remain in place and China has imposed a few of its own, but they are imposed on just $14bn worth of goods and appear to be largely of "face saving" symbolic value. Yes, things could escalate, but let's see what happens when Presidents Xi and Trump finally have a "chat".

At least Trump is not resorting to his worst-case threat of a blanket tariff on all goods for everyone. Calmer heads might be prevailing. He is next expected to unveil "reciprocal tariffs" on goods upon which the US is also subject to tariffs on its exports. Combined with the focus on individual categories (with steel and aluminum being the first), that is about as close as you can get to a surgical strike in a tariff war. Even so, our research analysts are going through every company under our coverage to assess the potential risks (and even rewards in some cases) and we will apply their findings to portfolios.

Immigration, or reversal thereof, is another big threat, although more localised. Migrants into the US (illegal or not) have contributed both supply (to the labour market) and demand (in terms of consumption). If the threat to deport 11 million of them was carried out in full, a big chunk of the economy would go missing, not to mention the cost of undertaking such a task, which I have seen calculated to be in the high hundreds of billions of dollars. After all, it's not as though they are going to walk home of their own volition. To put some numbers on the potential disruption, the day following a raid by Customs and Border Protection (CBP) on a citrus farm in Kern County, California, 25% of its workers failed to show up for work. On the second day it was three-quarters of workers who stayed away. Even documented workers felt vulnerable because the CBP is trying to fill arrest quotas and so taking people who just don't have their papers to hand. One assumes these workers can't stay hidden forever, but it's still disruptive.

The industry alongside agriculture that has a high proportion of migrant workers is construction, where there was already a shortage of labour relative to the demand. Migrants are believed to account for a quarter of the sector's workforce, with undocumented ones being a fair proportion.

What the tariffs and immigration controls feed through to is the possibility of a combination of weaker economic activity and higher inflation, a toxic combination at the best of times. The inflationary risk has been recognised in the shift in interest rate expectations, with far fewer Fed Funds rate cuts expected now than last summer (before the Trump bandwagon started to gather pace). Yes, the US economy has also been very resilient, but the policy effect has been instrumental too.

Much depends on how one views Trump's favoured outcomes. Is he really so ideologically motivated as to carry out his policies to the ultimate degree, or, as in the past, will he be satisfied with extracting deals that make him look like a winner? One phrase associated with Trump 1.0 was that he should be taken "seriously but not literally". There's obviously a possibility that that errs more towards the literal this time around, but the evidence so far does not point to that. It remains all about the underlying direction of travel and chalking up the "W"s. Even so, I would admit that he has come out of the gate very quickly this time in terms of invoking emergency measures and issuing executive orders. Trump looks like a man in a hurry and seems to enjoy the attention that every tweet and off-the-cuff remark attracts. Thus, I'm afraid there is going to be an awful lot more of this noise.

On a more positive note, I try to see external fund managers (FMs) when I can because it's good to get a break from all the macro commentary, which tends to focus more on the risks than the rewards these days. It's in (most) FMs' blood to focus on positive possibilities. I spent an afternoon last week with the FMs of a well-regarded London-based global fund manager and it was a breath of fresh air. Yes, I know it's part of their job description to encourage us to buy their funds, but they were realistic about the macro challenges while building portfolios of companies that offer various combinations of innovation, growth, safety, cashflows, dividends and share buybacks and all at a sensible valuation. And they are trying to focus on opportunities that lie well into the future rather than worrying about the next tweet. We regularly use a chart that shows the positive long-term progress of equity markets labelled with all the negative events that have occurred. When nerves are on edge, it acts as a good suppressant to the temptation to be hyperactive in terms of portfolio management.

Economic Commentary

FTSE 100 weekly winners

Fresnillo PLC	9.9%
International Consolidated Airlines Group SA	8.4%
Ocado Group PLC	8.4%
Coca-Cola HBC AG	8.0%
Entain PLC	5.0%
BT Group plc	5.0%
Antofagasta plc	4.7%

FTSE 100 weekly losers

Diageo plc	-8.1%
Croda International Plc	-8.1%
JD Sports Fashion Plc	-7.7%
Ashtead Group plc	-6.2%
Halma plc	-5.9%
DCC Plc	-5.3%
Barratt Redrow plc	-4.5%

FTSE 100 index, past 12 months

EuroStoxx 600 index, past 12 months

S&P 500 index, past 12 months

All data shown in GBP.

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