



HANSA CAPITAL GROUP

Hansa House View



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As at June 2025

2025



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Donald's Deal or No Deal

Like any good gameshow host, President Trump continued to keep the world guessing this quarter with 'liberation day' the key event from a market perspective. Trump announced tariffs on countries around the world, both allies and foes, based on a formula that can be distilled to their balance of trade for goods with the US. Using this overly simplistic view of trade, the Trump administration proposed a range of 'reciprocal tariffs' for countries around the world with a minimum global tariff of 10%. Markets unsurprisingly reacted negatively to this announcement with sharp declines seen in all major markets.

Ever the showman, this was intended as the starting point of Trump's grand re-negotiation. Being a self-described master negotiator, Trump always likes to go in with a maximalist approach before settling somewhere in the middle. The reaction from markets persuaded him to delay the implementation of the tariffs to allow time for negotiation with most countries willing to acquiesce to some degree. Where these negotiations ultimately end up is still uncertain but markets have responded positively to the apparent softening of Trump's opening gambit.

In a more volatile world the question of portfolio positioning becomes increasingly pertinent. As long term investors we have a default position of being fully invested, predominantly in equities. Our time horizon allows us to ride out volatility which is what we thought the market reaction to 'liberation day' was. We have long favoured the US market due to its entrepreneurship, innovation and willingness to change when needed. All of these advantages remain but we are concerned that higher valuations and its populist pivot make it less attractive than it was.

So, what are the alternatives to US equities? Europe has the same, well-rehearsed problems (it lacks entrepreneurship, innovation and a willingness to change) with its debt levels and Germany's struggling manufacturing sector being key impediments. However, Japan is making the necessary corporate governance changes which appear to be having an impact. We also think emerging markets look more attractive with relatively lower debt levels and a weaker dollar the catalysts. All benefit from valuations at a lower starting point than the US which provides a larger margin of safety. Higher yields have also made bonds a more viable investment option though high developed market debt levels and tight credit spreads give us pause for thought. We have, however, looked to add some exposure in this area.

Trump's penchant for unpredictability will inevitably lead to more volatility during the remaining years of his presidency. However, the strength of the US economy and its inherent advantages lead us to believe that it is still likely to be the best option for long term investors. However, we will continue to look to diversify the portfolio by country, style and asset class in the acknowledgement that other areas are looking more attractive and the US is not quite the no-brainer it once was.



From hero to zero.....

At the time of writing last quarter's House View the world seemed a very different place. Trump had gone from hero to zero as the market absorbed the impact of his tariff programme, culminating in his 'liberation day' announcement where he unveiled a swathe of tariffs that shocked the world in both size and scope with few escaping his wrath. Whilst the base level tariff was 10%, countries such as China saw tariffs as high as 34% and up to 50% for the highest tariffed countries. Markets unsurprisingly went into freefall, delivering the steepest falls since the onset of the COVID pandemic.

Like a gameshow host, Trump unveiled his global tariffs on 'liberation day' in early April



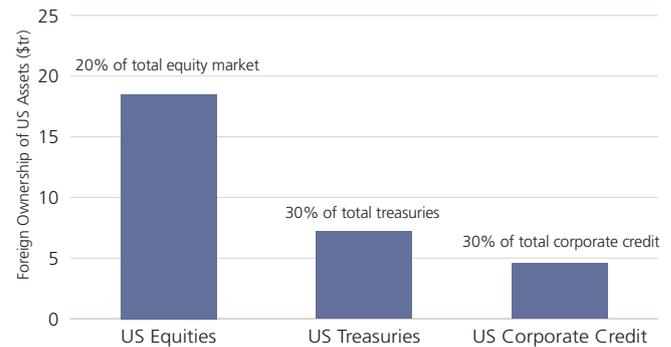
Source: The Guardian

On the face of it, these falls appeared justified. Trump had gone from a chaotic and largely rhetoric-based leader in his first term, to one who appeared to have found ideology and was pursuing his goals with conviction. With some justification, he was of the view that much of the world was profiting at the expense of the US, applying inequitable trade policies and expecting the US to act as the policeman to the world both from a spending perspective but also with boots on the ground. He believed in a weaker dollar, lowering surpluses and other countries picking up the baton in terms of both their spend on defence budgets and lessening the US's role in other people's wars.

In the first instance, the levying of tariffs was seen as likely to cause a stagflationary decline in growth, and probably a recession, and higher prices as tariffs were passed on to the end consumer. To many, however, Trump's actions looked like the beginning of the end to 100 years of US hegemony. The US, which had arguably been one of the biggest beneficiaries of globalisation in terms of lower prices and access to cheap goods, was seen as potentially the greatest loser from its retreat from the global stage. Moreover, Trump's actions started to bring into question the trustworthiness of the US. With significant proportions of the US dollar, equity and Treasury markets

being held by foreigners, any pullback on this front could be catastrophic for US assets, especially in view of their higher valuations versus the rest of the world.

Chart 1: Significant proportions of US Stocks, Treasuries and corporate credit are owned by foreign investors who may be spooked by Trump's rhetoric



Source: Federal Reserve, MacroBond, Apollo Chief Economist

We, however, took a more benign view of these events. Partly this reflects the fact that whilst markets tend to swing from one extreme to another, the reality is often more nuanced. We do believe that Trump has more conviction this time around compared to his first term. Then, he appeared to be as surprised as the next man that he had gained power and was ill-prepared to both form a government and to execute a coherent strategy. In contrast this time around he has hit the ground running, forming a government that is aligned with his beliefs and launching policies to enact them. Nonetheless, our contrarian view reflected the fact that whilst Trump may have more conviction this time around, he remains a dealmaker at heart. Whilst he may enter negotiations asking for more than is reasonable, ultimately he backs off when markets start to go into freefall or as systemic panic rears its head. This was the case in his first term and appears to be exactly the same model he is applying again – go in hard and backtrack at the 11th hour. Precisely the wrong action in such a situation would be to panic after the event as this almost inevitably leads one to being whipsawed by the rebound.

The other reason for our differing stance is far more fundamental. For years the naysayers have been calling the end of the US revolution – it's too expensive, too much money has been thrown at AI, the dollar is overvalued, other markets are much cheaper, and the list goes on. These criticisms, however, ignore the simple fact that the US has been so much better than most other countries in many key areas. Its valuation has been higher than other markets simply because its companies have been so much better and generated higher returns. Through entrepreneurship, a desire to do business and the ability to change at points of stress have all driven US profitability to levels which have justified these higher valuations. Similarly, the US consumer continues to confound the critics. Time and again, when people are questioning whether or not the US consumer will draw back their horns, they have continued to spend with a vengeance.



Chart 2: The return on equity has been much higher in the US compared to the rest of the world justifying the higher valuations



Source: Bloomberg

Conversely, bad markets do not become good markets overnight. Ultimately, the reason why markets such as Europe have struggled is that in contrast to the US their corporate returns have been poor. Through a lack of entrepreneurship, poor government policy, thin capital markets, and an overdependence on markets such as China, these are challenges that will take many years to change and not something that can be achieved overnight, if ever.

Hence, we remained far less cautious than many commentators on the US, despite Trump's actions at the end of the first quarter, and we simply did not see the worst-case scenarios playing out for equities, at least in the near term. Hence, we remained true to our long-term approach by not panicking out of markets nor rapidly rotating from the US.

Chart 3: Markets have rallied strongly in the last quarter after a significant fall around 'liberation day' in April



Source: Bloomberg

Outlook.....

Despite our rather sanguine positioning, it is important to note that we do agree that the world has become a very different place. The last couple of decades were clearly a golden period for markets. Characterised by the rise of China, global economies benefited from cheap goods, diminishing inflation and falling interest rates. This in turn resulted in an abundance of capital helping to facilitate the creation of companies, especially in the technology space, and propelling stock markets ever higher.

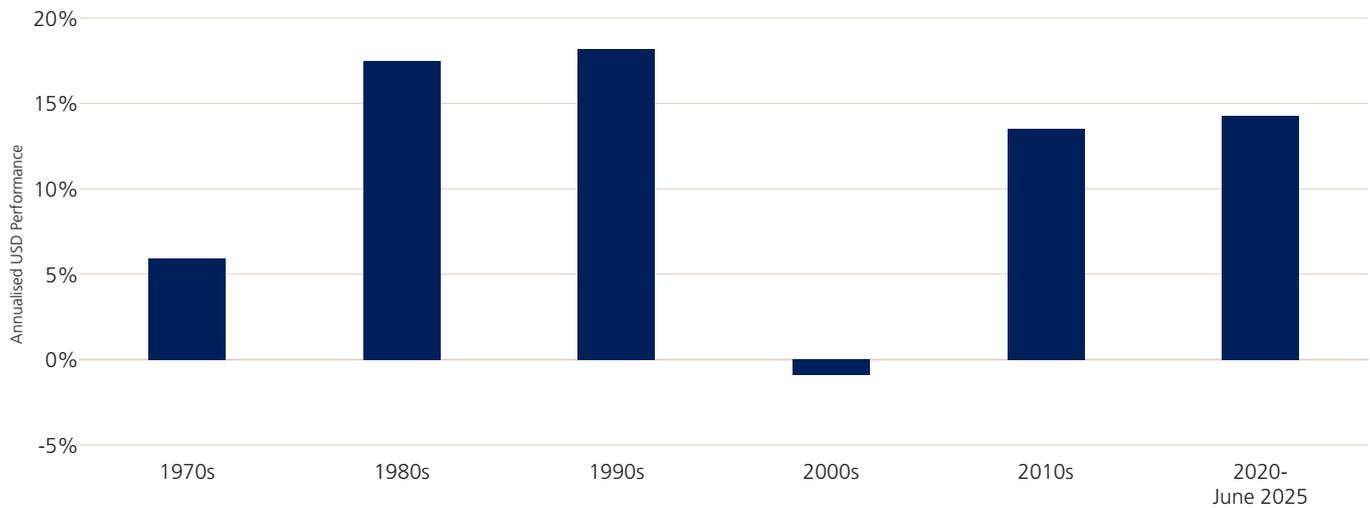
This period appears to have now ended. With COVID acting as the catalyst, globalisation lost its momentum as countries sought to either diversify their supply chains or reshore key industries. Trump's tariff programme has added fuel to this process as countries further retreat from global trade and become more inward looking.

The fear is that this both weighs on growth and is inflationary and, importantly, prevents central banks from throwing liquidity at markets as they have done at the first whiff of slowing growth in the past.

Hence, whilst we're not in the camp of believing that we are entering a stagflationary funk or that the US has suddenly lost its mojo, we do believe that the supernormal returns achieved over the past couple of decades will be far harder to come by, especially given the high starting valuations in the US. We're still of the view that if you were to buy just one market and go away for a decade, the US would remain top of the list. It's just that we think the returns will be somewhat lower and more volatile.



Chart 4: The US equity market has performed exceptionally strongly in multiple decades with the 2000s the notable exception

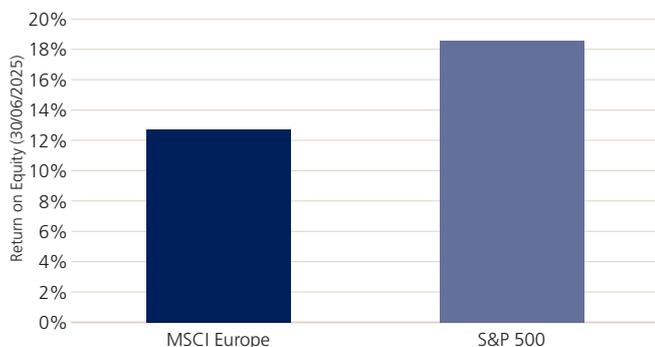


Source: Bloomberg

The other major global markets – Europe, the emerging markets and Japan – are more nuanced albeit have lower valuations in common. Europe, we remain to be convinced by. Whilst low valuations do provide areas of interest, we see little evidence that there will be a wholesale shift towards companies which generate consistently higher returns and even less convinced that Europe will develop their answer to the Magnificent 7 any time soon. Europe’s largest economy, Germany, has the added challenge that whilst much of its past success was based on manufacturing and exporting to China, increasingly China is looking to become more self-sufficient and now domestically produces many of the goods that were previously seen as the domain of Germany. The decision by Germany to relax its deficit rules and its €1tn “whatever it takes” spending plan for defence and infrastructure gives considerable hope but time will tell if these words flow through into genuine action. The labyrinthine bureaucracy of the EU and internal politics in Germany are considerable hurdles to overcome that may ultimately lead to the money being poorly spent.

Emerging markets and Japan are potentially more interesting. We’re not in the camp that believes that the emerging markets can be bought and held forever. With a few exceptions, most emerging economies have periods of strength only to see these gains given up as political turmoil, poor governance and a lack of the rule of law reappear. Nonetheless, there are periods when the emerging markets can do well and sometimes these periods can last for a protracted period of time, just as was the case in the mid-2000’s as China started its journey towards the powerhouse that it is today. Potentially we may be entering one of those periods now. Valuations are low following what, for many emerging markets, was a lost decade and a half. The financial positions of many emerging economies are the envy of the developed economies. Largely this was a function of necessity with the emerging economies not afforded the luxury of running large deficits and borrowings as has been the case for the developed markets. Perhaps most importantly, the dollar is weakening. Historically a weaker dollar goes hand in hand with strong EM performance as dollar linked borrowing costs fall, dollar import costs diminish and, typically, with the rise in commodity prices which is normally associated with a weakening dollar. The key question is whether this is yet another head fake with the demise of the dollar yet again overplayed with few real alternatives for global cash. Whilst the dollar does appear overvalued on a Purchasing Power Parity basis, in reality few investors are going to want to hold significant proportions of their assets in alternatives such as the renminbi or the euro which have their own challenges. Gold undoubtedly has an attraction, but, by virtue of its limited supply, will always be capped in its role within the global monetary policy framework.

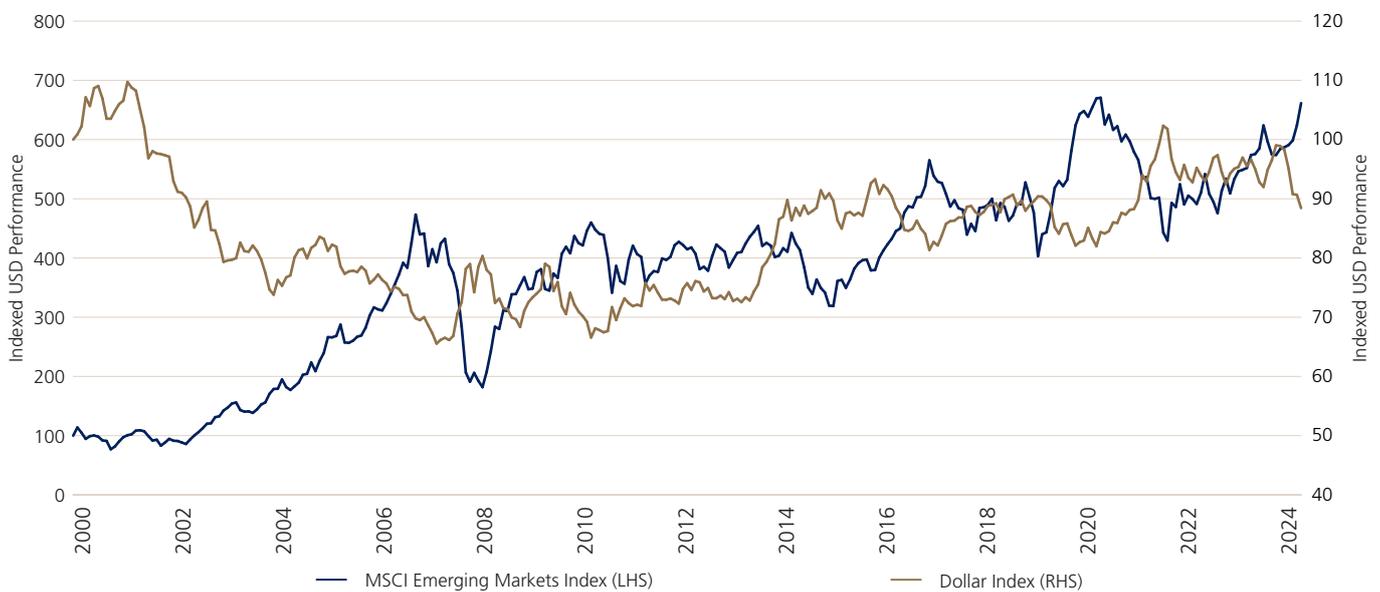
Chart 5: The return on equity in Europe is notably below that of the US



Source: Bloomberg



Chart 6: Emerging markets typically perform more strongly when the US dollar is weaker



Source: Bloomberg

In many ways Japan represents the direct inverse of the US. Where the US has benefited from entrepreneurship, innovation and a willingness to change when needed, Japan has been characterised by a resistance to change and companies which were weighed down by complex cross-shareholdings and excessive levels of cash. Hence whilst the US has gone from strength to strength over the last 30 years, Japan never took the hard actions required to purge the excesses of the eighties resulting in three decades of stagnation.

Increasingly though, there has been a growing recognition within Japan that radical change is required, especially in light of the twin structural threats of an ever more powerful China and an aging population that is straining Japan's labour market and social security system. Hence, a number of important changes are being enacted, ranging from the unwinding of the complex holding company structure and forcing companies to eliminate excess cash levels. This programme of rejuvenation will take time with many of Japan's problems structural but we are starting to see the fruits of their efforts with improving returns versus the rest of the world and companies paying out excess cash and selling non-core divisions. Activism, which for years was resisted within corporate Japan, is now playing a much more important role and, with government efforts to encourage the purchasing of equities, the outlook is looking rosier, especially in light of low valuations.

Shareholder activism is increasing in Japan which is leading to a higher return on equity

Japan firms face record activist shareholder proposals, raising reform pressure

Activists push Japan Inc to its 'great tipping point', says Suntory head

Management booted out as Japan's shareholders flex their muscles in AGMs

Source: Reuters, Financial Times

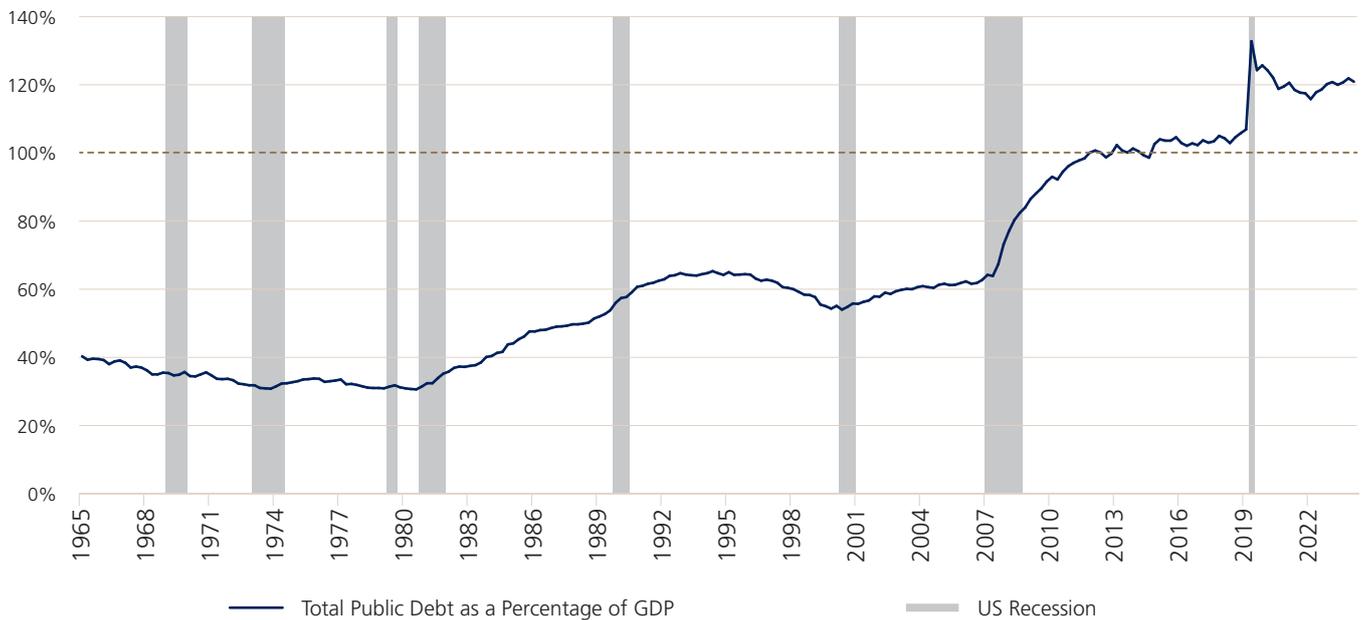
Tail risks.....

More seriously, Trump's actions have the potential to catalyse some of the more sinister tail risks within markets.

On the one hand, US debt levels look worryingly high. Like many countries in the developed world, US government policy shifted from a counter-cyclical approach where policy was loosened at points of cyclical weakness, to one of spending exceeding income irrespective of the cycle resulting in ever increasing debt levels. Trump's answer to this seems to be based on a pro-growth agenda centred around fiscal stimulus and haranguing the US Federal Reserve to cut rates. It is not inconceivable however that his policies have precisely the opposite effect. Spending more and cutting taxes will likely make the deficit situation worse in the near term, which, combined with potentially slower global growth due to his tariff programme, will only serve to exacerbate the US debt problem. With international investors potentially pulling back from funding the US market, this raises the spectre of a crisis in confidence and a disorderly unwind. In practice there are a number of safety valves linked to the dollar's reserve currency status and the ability to print more dollars but Trump is playing with fire.



Chart 7: US debt levels are becoming an ever larger portion of GDP and no longer only increasing during recessions



Source: FRED, Bloomberg

The other issue we worry about is a geopolitical misstep. Trump campaigned on an agenda of pulling the US back from the global stage, both monetarily and militarily. Despite this he seems unable to resist engaging in areas of conflict and, contradicting his rhetoric on withdrawing from the global stage, his recent decision to bomb Iran seems to suggest otherwise.

Our fear is that the combination of Trump's unconventional negotiating style and the shifting sands as countries such as China and India grow in size and military might, raises the prospect that a flare up gets out of hand. History suggests that this is a risk that should not be underestimated.

Chart 8: While the US remains the globally dominant military, China is rapidly catching up in some areas

		 Aircrafts	 Tanks	 Navy Fleet	 Military Budget 2024 (\$bn)
	United States	13,043	4,640	440	968
	China	3,309	6,800	754	235
	Russia	4,292	5,750	419	145.9
	Germany	584	296	61	86
	United Kingdom	631	227	109	81.1
	India	2,229	4,201	293	74.4
	Japan	1,443	521	159	53

Source: The Military Balance 2025, Global Firepower



Action points.....

Distilling this backdrop down to the portfolio level is challenging! Trump relishes chaos and just when you think you can see a path

through the chaos, he will come back with another curveball. Nonetheless, our long-term approach gives us a clear advantage over our peers, many of whom are forced to attempt to call markets in the short-term.

1

Retain an overweight position in equities

Many times we have stated that a strong bias towards equities is essential for long-term investors such as ourselves, where we are trying to preserve and grow the spending power of money through tying our returns to the growth of corporate earnings. Occasionally we will pivot away from equities but the hurdle for doing so is high.

Hence, whilst we see the future under Trump as a volatile one, and with returns over the coming decade likely to be somewhat lower than the past, we remain of the view that it is correct to retain our overweight stance in equities.

2

Adding diversification at the country level

As discussed above, the US retains a multitude of structural advantages that underpin its stock market. It remains our favoured economy and stock market by a wide margin.

However, we also acknowledge that Trump has created considerable uncertainty and added to the risks facing the US economy. In contrast, whilst many other markets are challenged by Trump's actions, their valuations are lower and, in recognition that Trump is hard to trust, more self-help measures are being put into place. It is for this reason that we are increasingly looking to judiciously add to positions in the emerging, Asian and Japanese markets.

3

Diversification at the style level

In a world of low inflation and low rates, growth investing has the twin advantages of both getting a premium for the growth generated but also lower financing costs with cheap money used to fund companies in capital intensive growth sectors such as technology and biotechnology.

In contrast, in a world of higher interest rates and inflation, the case for growth still exists, but becomes less compelling. With lower valuations providing a margin of safety in a more volatile world, we now look for a blend of both value and growth.

4

Add diversification at the asset class level

One of the main differences between the deflationary backdrop of recent years and a more inflationary environment has been the return of positive yields. In a zero-interest rate world, bonds became an extremely unattractive asset class in our opinion. We saw the risk profile as skewed to the downside unless markets remained deflationary forever.

Now, with yields at higher levels, and indeed with positive real yields, bonds are becoming a viable asset class again. We do not however think that they are a blanket purchase. As highlighted above, many developed economies are highly indebted and any loss in confidence may lead to a disorderly unwinding. Similarly, credit spreads remain very tight by historical standards and provide little protection to a rise in the current low default rates. Even so, there are areas that look interesting and we have identified two excellent bond fund managers to dynamically play these opportunities. We will likely be searching for more names in this space.

An area that is perhaps less suited to the current environment are the CTA managers. These funds target share price momentum and, historically, when combined with equities have produced better returns than the classic 60:40 equity:bond portfolio. Unfortunately, volatile markets can be their nemesis with the funds being caught in the initial sell-off only to be whipsawed in the rebound. Time will tell if markets eventually become immune to Trump's bluster but it seems likely that the rest of his term will remain a volatile one. Hence, this area is likely to be a source of cash for us.



Summary.....

Yet again Trump has thrown the cat amongst the pigeons. Having shocked the world with the scale of his tariff programme, sending markets into turmoil in the process, he appears to have reverted to type and backed off at the last minute. Holding our nerve, playing to our long-term strengths, and resisting capitulation at precisely the wrong point served us well. The key question now is whether Trump comes back for another go (probable in our view) and if his actions ultimately cause a downturn or, worse, a recession. Fortunately, the US economy is starting from a position of strength albeit time will tell if this is enough to ward off the worst of Trump's actions.

Portfolios need to be managed very carefully in this backdrop and a tried and tested process is essential. No longer are we underpinned by the rising tide of falling inflation, low rates and abundant liquidity. Instead, we need to contend with the vagaries of one individual in a world where the geopolitical situation has become increasingly unstable. Nonetheless, we are blessed by the length of our investment horizon and not being required to mindlessly track indices. Diversification will be key in such a backdrop, something which we are well placed to apply at Hansa given our expertise across geographies, sectors and asset classes.

Alec Letchfield

July 2025

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