

Cognitive drain

23 September 2025

I was listening to an interview with Helen Thompson, a Professor of Political Economy at the University of Cambridge, last week. She came up with a perfect phrase to describe the world in which we now live: “Cognitively draining”.

I suspect we all feel the pressure on our mental faculties in some way. Many of our concepts of what constitutes the *status quo* are being rewritten, but that’s not the only issue. We’re subject to a constant barrage of information, misinformation and downright propaganda from which it’s difficult to detach ourselves, especially if we have the responsibility of safeguarding clients’ wealth.

Somewhere in the distant past I read a book about information theory. One point that always stuck with me from it was that filtering out the information that we don’t need is in itself a hugely energy-intensive process. But that was written well before the internet had become embedded into our daily lives – and even longer before the dawn of smartphones and social media. Is it any wonder that uncertainty indices are at all-time highs and consumer confidence appears permanently fragile?

Quick take:

- Corporate profit growth and strong liquidity are boosting stocks and other risk assets
- Rising US wealth is supporting consumption
- Tax changes could further boost US spending

And yet, despite all this anxiety, risk assets such as equities are hitting all-time highs. Moreover, credit spreads – the extra yield over government bonds demanded by investors to invest in corporate bonds – are close to all-time lows. Then again, gold, seen as the most credible all-weather risk-diversifying asset to add to a balanced portfolio because it tends to rise when nerves about the global economy are shakiest, is also at an all-time high. If you’re confused, you’re not alone.

Pluses and minuses

Many competing forces are at work here. For me, the most concrete positive ones are corporate profit growth and benign liquidity conditions. The more nebulous

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ones are the promise of an increase in productive growth through the adoption of artificial intelligence (AI) and the fear of missing out (Fomo) that tends to grow as bull markets extend. On the negative side are (geo)political concerns and worries about the sustainability of government debts in most developed economies (and what that means for taxes). There are also stretched equity valuations (mainly in the US) and a fair amount of fretting that all the capital investment in AI might fail to pay off.

I've covered all these subjects individually in various commentaries so I'm not going to go through them all in detail again. But I can add a bit more colour on a few aspects, starting with what is probably the most important: the risk of a US recession. The Federal Reserve (Fed) has started to cut interest rates again. That tends to be associated with rising equity markets. But the exceptions – the times when stocks haven't risen – have been when a recession develops.

Recessions often result from higher interest rates, when a central bank is deliberately trying to dampen economic activity to reduce inflation. But when the Fed raised rates with that purpose in 2022, there wasn't one, even though an analytical model built by Bloomberg Economics, a research service, predicted a recession with 100% probability. There were a few important reasons for that.

One was that the government's fiscal stimulus remained powerful. Another was that much private sector debt, especially mortgages and corporate credit, had been fixed at very low rates in 2020 and 2021. For this reason, debt service costs rose very little. Finally, households and bigger companies still had plenty of cash in the bank, post-pandemic, because of furlough funding and (for households) shuttered shops. Suddenly that was generating a large amount of interest payments, which had not been enjoyed for years.

And then the AI boom started.

ChatGPT, the first publicly available generative AI application, was unleashed onto an unsuspecting world in November 2022. Since then, the US' S&P 500 Index has delivered a total return (including dividends) of 70%, while the tech-heavy Nasdaq Composite has doubled your money and the Indxx Artificial Intelligence & Big Data Index has risen 133%. But all those gains are eclipsed by chip designer Nvidia, whose total return is a staggering 945%. (All data is total return in US\$ as at 19 September 2025.)

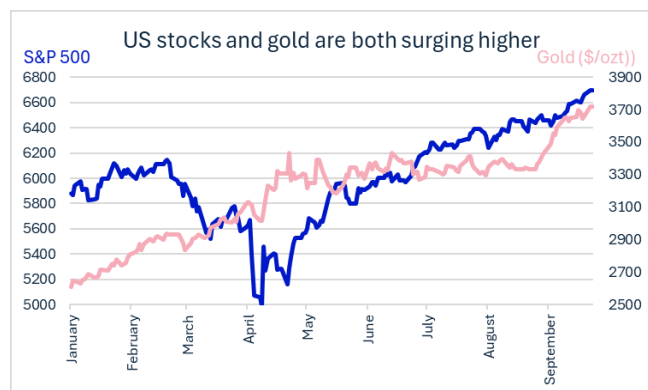
Major indices outside the US have underperformed in comparison. The FTSE 100 is up 52%, MSCI Europe ex-UK up 59%, Japan's Topix up 59% and MSCI Emerging Markets up 50%. On an annualised basis, these still represent

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gains far greater than their historical averages, but there is a strong feeling of envy on seeing how US investors have made out like bandits. Furthermore, non-US (retail) investors tend to have less exposure to equities.

Even so, one notable European stock has outpaced even Nvidia: German defence company Rheinmetall (+1,067%). If only its business of making the machinery and ordnance of warfare wasn't something else to give us sleepless nights...



Source: FactSet, Rathbones. Value of gold is per troy ounce, derived from LBMA afternoon pricing session.

Booming boomers

This has all had an impressive effect on US household wealth, although I'm aware that it's far from evenly, or even equitably, distributed. I'm also aware that changes in these household balance sheets have historically had a relatively small effect on household consumption, but there do seem to have been some behavioural changes among certain consumers,

notably older (and often richer) ones. Remarkably, almost 50% of consumption now comes from the wallets of the top 10% of households by income (which largely overlaps with the top 10% by wealth).

The US household balance sheet shows assets as nine times the size of liabilities. Assets are largely investments (60%) and homes (27%). Liabilities are dominated by mortgage debt (67%). Wealth inequality is rising, with all the political tension that comes with that. But for now, we focus on the positives of what economists call the 'wealth effect': how much household spending rises or falls as wealth does so. Changes in Q2 household wealth show an increase of almost \$7.1trn, bringing the total to \$167trn. That's the third biggest increase in history, in absolute terms.

And this all comes before the 7% gains for the S&P 500 this quarter so far and the 11% gain for the Nasdaq. No wonder Americans seem to be swarming around your favourite holiday destinations in Europe, forcing prices up, although probably less so now that the dollar has weakened.

Another thing that could support consumption further, into 2026, is the effect of tax changes made in the One Big Beautiful Bill Act. Tax cuts and changes to deductions passed into law earlier this year were backdated to 1 January. However, the Internal Revenue Service, or

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IRS (the US equivalent of HMRC), didn't change its calculation of withholding taxes – taxes levied before money goes into pay packets. That will mean bumper tax refunds paid in January 2026. The average refund was \$3,200 this year and JPMorgan calculates it will be \$4,000 next year. Monthly pay cheques will increase too, once the IRS starts to apply the deductions; the prime beneficiaries will be lower-income workers who have a higher propensity to spend what they earn.

We're far from complacent about the state of the US economy and the world in general, but we're not hiding under the metaphorical duvet. Even when one has concerns, it generally pays to stick with markets as they trend, at least if we cannot identify an immediate trigger to reverse that trend. We know, for example, that US equity valuations look high, as measured by valuations such as price-earnings ratios. But they also reflect some of the option value of the benefits of AI to come – a bet on the prospect that US stocks could deliver strong value in the future. They also reflect the potential for lower interest rates.

I often think that one of the primary roles of a wealth manager is to do the worrying on behalf of clients so they can enjoy the fruits of their hard-earned wealth. There has to be a great deal of trust in this relationship. I can assure you that we try to leave no stone unturned in our pursuit of the best possible investment outcomes given the circumstances, even if that can leave one cognitively drained at times.

For recent economic highlights, see below.

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UK – The Bank of England kept the base rate unchanged at 4% last week, much as expected. Earlier in the week, the Bank's challenge was highlighted by the still-elevated rate of inflation in August, with headline consumer price inflation (CPI) running at 3.8%. Services inflation of 4.7% did at least fall from 5%, but remains too high for comfort. More attention was paid to the Bank's decision on its balance sheet reduction (quantitative tightening) – it has decided to slow the pace from £100bn to £70bn a year – and to shift issuance of gilts to shorter maturities. This helps take some of the recent pressure off long-dated gilts but doesn't address the root cause: government debts are too high.

On that front, the latest data for the public finances was depressing: the deficit of £18bn was much higher than the expected £12bn. Higher interest payments and weaker-than-expected tax revenues were blamed. This piles further pressure on Chancellor Rachel Reeves ahead of November's Budget, especially with the Office for Budget Responsibility reported to be on the verge of cutting its forecast for trend growth in productivity (output per worker). This will lower forecast GDP growth unless there's a prediction of offsetting labour market growth. That looks unlikely in the face of current demographic trends and increasing resistance to immigration.

US - The Federal Reserve restarted its rate-cutting cycle with the first this year: a quarter-point reduction, to the 4 to 4.25% range. This was the first meeting to feature President Trump's interim appointee to the committee, Stephen Miran. Although he favoured a bigger cut and then more aggressive ones at the next two meetings, there was no sense of undue influence from the White House. Chairman Jerome Powell maintained his vigilant stance towards inflation risks, and inflation expectations priced in by markets remain pretty well-anchored, not so far from the Fed's 2% target. Signs of consumer resilience were seen in August's retail sales report, with month-on-month growth of 0.7% vs an expected 0.4%. Interest rate futures suggest another two quarter-point cuts in 2025, followed by a further two or three in 2026. This would take the effective rate – the actual rate in the market – to around 3%.

Europe - Despite a small improvement in the September ZEW index of Eurozone economic sentiment, there's scant evidence that the trade deal with the US has significantly lifted investor sentiment. July trade figures showed a normalisation in trade flows, with slower annual growth in exports following the surge driven by the front-loading of goods by US importers earlier in the year, ahead of tariffs. Trade with the US hasn't fallen off a cliff, but as 15% tariffs continue to bite, exports look

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set to remain sluggish. Eurozone inflation in August was revised down from its preliminary estimate to its target level of 2%. With the recent appreciation of the euro, inflation is likely to fall below target in the coming months. The strong hawkish tilt in the central bank's communication means the bar to another rate cut is high. But market pricing now suggests an increased probability, now at 50%, of another quarter-point reduction in the months ahead.

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