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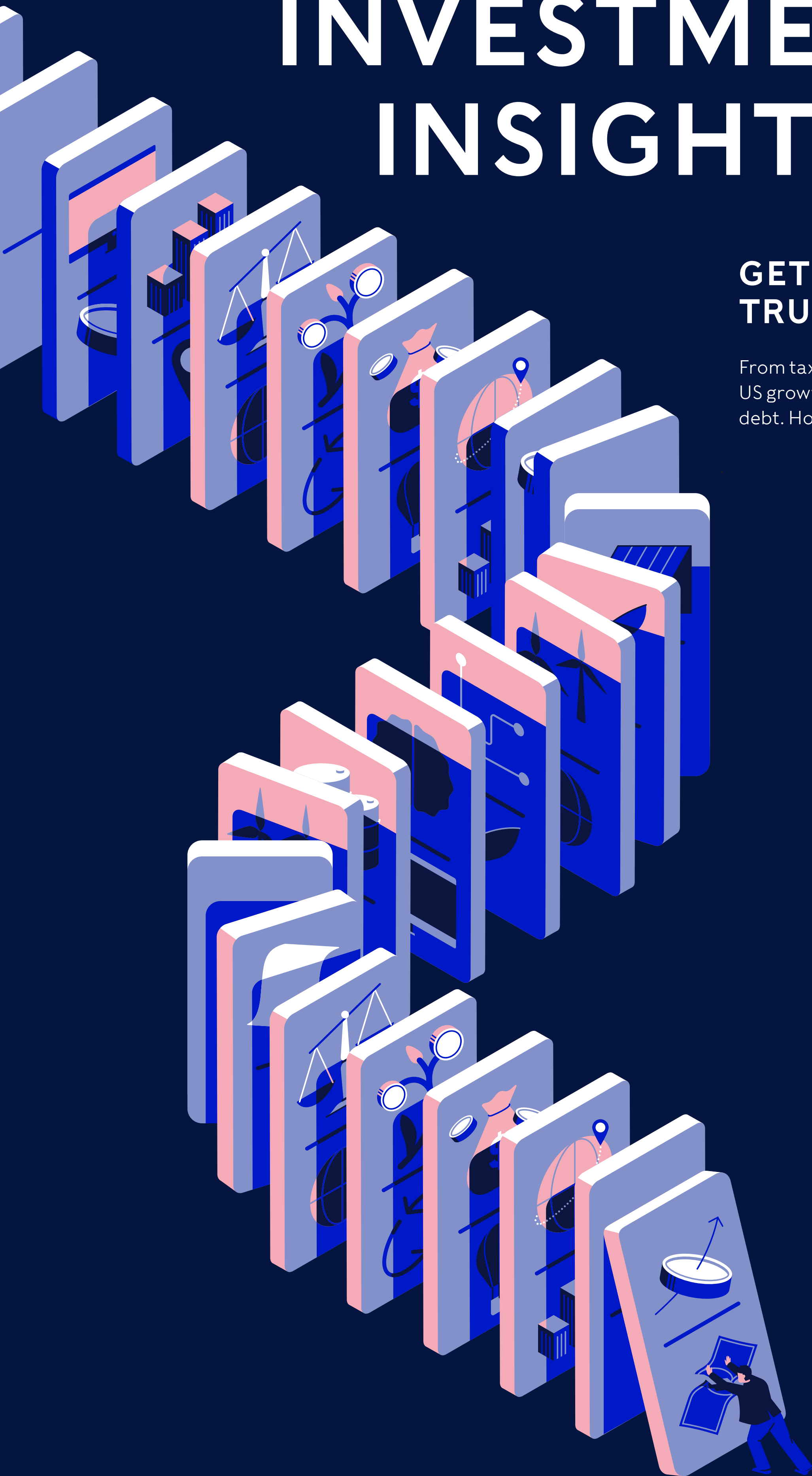
INVESTMENT INSIGHTS



GETTING READY FOR TRUMP'S SECOND ACT

From tax cuts to tariffs, a new agenda could bolster US growth and equities, while driving inflation and debt. How can investors navigate these challenges?

RATHBONES

FOREWORD

Investment Insights Webinar
Tuesday 11 February, 12.00 to 12.30pm
If you'd like to join our investment experts at our next Investment Insights webinar on Tuesday 11 February to hear more about the outlook for the global economy and markets.
To register, please visit www.rathbones.com/about-us/events

Welcome to the latest edition of Investment Insights. Events in the US continue to shape the global economy and financial markets, reinforcing the country's outsized influence. Throughout this edition, we examine the domino effects of key developments across the Atlantic and explore their implications for investors everywhere.

Our lead article on page 4 delves into Donald Trump's unexpectedly decisive return to the White House and the challenges of investing at a time of heightened policy uncertainty. We discuss how his second term could influence markets, from trade and taxation to technology and regulation, and the steps we're taking to navigate through this evolving landscape.

On page 6, we look at what has come to be known in the equity markets as 'American exceptionalism', and why US companies have been favoured over global peers. Their valuations are higher as a consequence, but we explain why we think they're still worth paying for.

On page 8, we shift focus to the rise of generative AI, a technology poised to reshape industries far beyond its origins in Silicon Valley. With tech giants pouring trillions into infrastructure, we've written again on whether these investments will deliver the higher revenue needed to justify the hype.

The inflation outlook takes centre stage on page 10. As structural forces look likely to increase the volatility of inflation and interest rates, we explore why we think the bond 'ballasts' in balanced portfolios should be shorter-dated.

Lastly, we turn to the future of ESG investing in the US on page 10. Trump's deregulatory agenda and expected retreat from climate commitments present new challenges. Yet, that doesn't mean the financially material environmental, social and governance risks (ESG) for some companies have gone away. Furthermore, as other global players step forward, opportunities for leadership in the green transition could emerge.

We hope you enjoy this issue and look forward to updating you in the coming months. We always welcome your questions about what's happening in the world today and how it affects your investments. If you'd like to find out more, please visit rathbones.com or get in touch with your usual Rathbones contact.

E. Savage.

Liz Savage and Ed Smith
Co-chief investment officers

WHAT CAN INVESTORS EXPECT DURING TRUMP'S SECOND ACT?

President-elect Donald Trump's political story is defined by unpredictability. From defying the odds as a outsider claiming the presidency in 2016, to becoming only the second US President ever to win non-consecutive terms in 2024, Trump has a knack for tearing up the script. That's before we get to his penchant for unfiltered social media posts, personality-driven dealmaking with other world leaders and rapid turnover of advisers. For investors, this situation creates a quandary. Trying to predict precisely what Trump will do is futile – yet we cannot afford to ignore him either.

Fortunately, there are still things we can do to prepare as the curtain rises on Trump's second act. Premising positions on specific policy changes under his new administration is foolhardy. But it is still possible to identify broad themes in his agenda – areas where the policies he is considering may work in the same direction. There are also lessons to be drawn from Trump's first term, including the issues he emphasised on the campaign trail and the interests of the lawmakers whose support he will need. We aim to reflect these themes through three key tilts in our portfolios. These positions are designed to prepare us for Trump's return, while respecting the uncertainty around individual policy decisions.

'America First', others last?

First, we are favouring US stocks over their peers elsewhere in the world, particularly those in emerging markets. Trump's 'America First' agenda only adds to the risks for markets outside the US, while it arguably contains some silver linings for domestic stocks. There are broader reasons, unconnected to the President-elect, to think that US stocks are relatively well-positioned in the near term.

Consider the potential impact of the much higher import tariffs Trump is proposing. True, they don't simply affect foreign firms trying to sell into the US, as 'tariff man' Trump sometimes seems to suggest. They're also a problem for US firms importing inputs, as we discuss below. But experience suggests the risks they pose to both economic growth and to stocks are greatest outside the US. (Part of the explanation is that the sheer size of the US economy means it's proportionally much less reliant on trade than any other major economy. Protectionism is more appealing if you have a huge internal market.)

China is again the primary focus of Trump's protectionist ire. He's talked about a 60% tariff on all Chinese imports, compared with the 10–20% rates he's considering on the rest of the world. That plan may well be watered down by lobbing or pared back through negotiations. But the direction of travel, and the focus on China, is clear. The principle of protectionism focused on China, if not Trump's specific plan, also has bipartisan support in Washington. That, and the experience of the start of the trade war back in 2018, suggests that stocks in China and emerging markets closely tied to it are most vulnerable.

On a different note, there's the idea floated by the Trump campaign of cutting the headline rate of US corporate tax from 21% to 15% (whether across the board or just for certain sectors is not clear). Trump has already been here, cutting the rate from 35% to 21% during his first term in office. A further cut is far from guaranteed. But if it happened, it would be a tailwind for stocks that pay tax in the US specifically, favouring the US market. If you don't pay corporate tax in the US, you don't benefit.

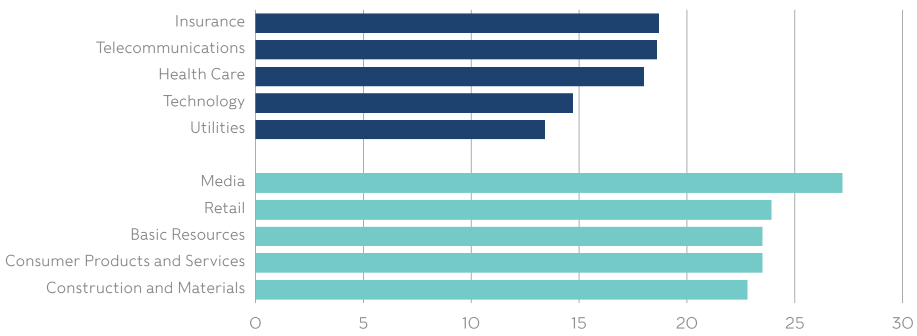
Then there's the fact that the US market has the wind at its back for other reasons. Analysts have been revising up their expectations for profits in the US by more than in most other markets recently, reflecting both the relative strength of the US economy and its exposure to the structural theme of artificial intelligence. The US also has a particularly high proportion of companies with the 'quality' characteristics we typically look for in our investments.

These are factors linked to long-term performance, which tend to indicate a company will be more resilient in the face of volatility. They include strong balance sheets, high and stable profit margins, and a track record of efficient investment. We explore the rationale for allocating to the US stock market, and the issue of its valuation, in the article *American exceptionalism*.

Figure 1: Assessing corporate tax cuts

This chart shows the effective tax rates for the top and bottom five sectors in the S&P 500 (excluding real estate). The greatest beneficiaries of any corporate tax cuts are likely to be the companies that pay the highest proportion in the US, such as media and retail businesses.

Source: Factset and Rathbones



Lastly, it's worth stressing that the day-to-day political 'noise' associated with Trump's leadership isn't a good reason to avoid US stocks. They delivered historically strong annualised returns of 14% in his first term, despite endless controversy and even Trump's own impeachment. Markets have proved good at looking through this noise, and part of our task as investors is to detach ourselves from the politics.

Changing of the guard

Second, *within* the US stock market, we are tilting away from the tech titans, which have been the biggest winners of the past few years. While these giants should still play an important role in portfolios, the balance of Trump's agenda adds to the broader case for allocating to smaller firms and suggests sectoral leadership could broaden out.

Take the issue of corporate tax cuts as an example. The greatest beneficiaries are likely to be the companies that pay the highest proportion of their tax in the US. Many large tech (and pharmaceutical) companies would gain little or nothing at all. That's because they report a substantial share of their profits in lower-tax jurisdictions overseas, such as Ireland. The median tech firm in the S&P 500, for example, already pays an effective tax rate below the 15% level to which Trump is proposing to cut the US headline rate (figure 1).

When it comes to the tariffs Trump is proposing, China is the largest target. That may be a particular problem for firms with a high proportion of Chinese suppliers. Our analysis of supply-chain data suggests the largest tech hardware and retail firms are particularly exposed, along with the car, chemicals and industrials sectors. In contrast, sectors like banks, real estate, media, insurance and utilities appear relatively insulated.

More generally, Trump's platform probably creates greater short-term risks to economic growth *outside* the US than in, which favours firms making a higher proportion of their sales on American soil. Again, within the US market the largest tech firms score near the bottom on that count. Across sectors, smaller stocks typically make a greater share of their money in the US.

Markets have recently begun to move in this direction. Having blown away the competition in 2023 and the first half of 2024, the so-called Magnificent Seven stocks have collectively underperformed the rest of the US market since July. However, with the valuations of smaller companies still low compared with that of their larger peers, a potential long-term investment opportunity still exists.

Protecting against inflation

Third, we are allocating to inflation-protected US government bonds (known as TIPS), and specifically to those that mature relatively soon. This strategy is designed to guard us against the various inflationary aspects of Trump's agenda, while also providing a reasonable return. Although inflation in the US is now back below 3%, several elements of what Trump is proposing arguably add to inflationary risks, notably tariffs and reduced immigration.

Short-maturity TIPS are particularly well suited to protect us against higher-than-expected US inflation. By design, their cashflows rise in line with inflation. That's also true of longer-maturity TIPS, but the experience of 2022 shows that in practice they provide less effective protection against inflation. Their prices are much more sensitive to changes in investor expectations for interest rates, which often also move a lot when inflation is rising. Many short-dated TIPS also offer real yields (after inflation) of around 2%, in stark contrast to much of the past decade when real yields were routinely negative (figure 2). Therefore, we're getting inflation protection and the prospect of a reasonable return to boot.

Further reading

Find out more about the potential implications of Trump's policies in our special report *Polls Apart* by visiting our online Election Hub at www.rathbones.com/rathbones-election-hub-financial-insights-2024-elections

Figure 2: Protection from inflation

This chart shows the real yield of the 1- to 5-year US TIPS index (%). Short-maturity TIPS are particularly well suited to protect our portfolios against any unexpected increase in US inflation.

Source: LSEG and Rathbones

IS IT WORTH PAYING MORE TO INVEST IN THE US MARKET?

As we continue to seek the best possible portfolio returns for clients, US equities are playing a greater role. This view is not just based on the strong performance that they've enjoyed in recent years, but also on the many attractive characteristics they hold for the future.

Much of this dominance stems from the exceptional returns generated by a relatively small number of companies, but markets in other regions have lagged too. Europe's heavy weighting to financial companies proved to be a drag following the two-punch combination of the global financial crisis and the eurozone crisis. Meanwhile, China's positive influence on emerging markets in recent decades has been undermined by the bursting of a speculative real estate bubble. Only Japanese equities, among major developed regions, have offered comparable returns to the US market, when measured in local currency terms, but at the expense of a very weak yen.

An abundance of resources

That is all water under the bridge and we need to focus on why it still makes sense to allocate more to the US. In terms of raw material, the US is well placed. It is rich in natural resources, has a growing population and a huge domestic consumer market, which offers immediate economies of scale. Its core financial system provides plentiful liquidity (an abundance of buyers and sellers) and the wider financial community has the sort of tolerance for risk that has helped to breed innovation (often with a helping hand from government agencies or academic institutes). The regulatory environment is usually fair and corporate governance is strong.

This is the background against which the world's largest companies have been born and then thrived. The current crop, which includes Apple, Alphabet (formerly Google), Amazon, Meta (formerly Facebook) and Microsoft, have developed platforms and networks with global scale. Their extraordinary profitability allows them to continue to invest in future growth. Along with companies such as Nvidia and Broadcom, they are now pushing forward the boundaries of artificial intelligence. The US leads all other countries by some distance in the development of data centres.

One area where we might justifiably receive some pushback is on valuations. US equities look expensive compared with their global peers. Prices relative to earnings are also high by historical standards. However, if we use less blunt instruments to value companies, the numbers look more favourable. A key metric is the cashflow that companies get in return for their invested capital, and the more highly valued companies benefit from having stupendous cashflow (figure 3).

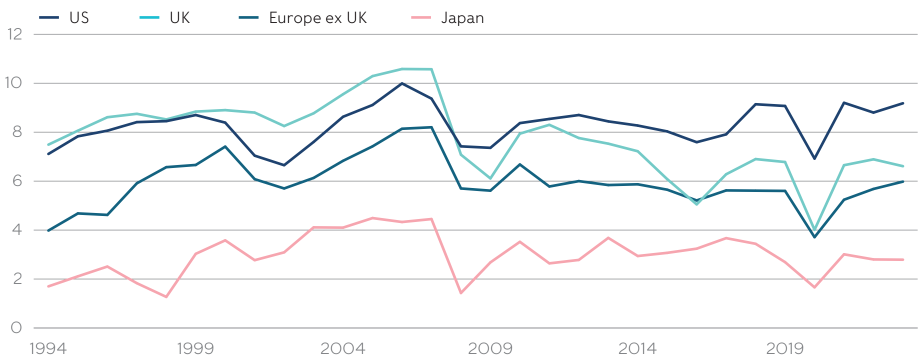
Weighing up the risks

Comparisons with the technology boom and bust at the turn of the century are misleading owing to the profitability of today's tech titans. We are not oblivious to the risks. The need for mega-cap tech firms to spend on capital is rising from historically low levels due to investment in generative AI (think huge amounts of Nvidia's chips). The ratio of free cash flow to revenue for these firms has started to come under pressure since the middle of the year, when their stock prices stopped outperforming the broader index. As a rule, investors tend not to reward companies with rising capital needs and falling margins, but mega-cap has been given a free pass. This poses a risk, as we discuss in the next article on page 8.

Profitability could also be undermined by, for example, higher employment costs or increased taxes. We acknowledge that labour's decreasing share of corporate profits is one of the reasons behind rising inequality and the prevalence of what we might broadly describe as 'populist' politics. Yet the risks on this front appear to be greater on this side of the Atlantic. Of course, we will continue to invest in companies outside the US where they offer a 'best in class' investment solution at the right price.

Talking of politics, what of the outlook for the second Trump presidency? While we might not like the way he goes about things, we have to concede that his 'America First' approach is designed to bolster the domestic economy. That is why we think there are also attractive investment opportunities further down the pecking order among the higher-quality small and medium-sized companies.

Figure 3: Cash flow return on investment (%)
Relative to other regions, many US companies deliver extremely high cash flow relative to the amount they invest in capital.
Source: USB HOLT and Rathbones

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GENERATIVE AI NEEDS TO GENERATE MORE REVENUE

The world is witnessing the greatest explosion of investment in technological infrastructure since the telecoms boom of the late 1990s. This time, instead of laying the fibre to connect the internet, large US technology firms are spending colossal sums of money buying Nvidia chips to run generative artificial intelligence (AI) applications.

By the end of 2024, Nvidia will have sold almost $200 billion worth of AI chips and industry analysts estimate this figure will have risen to $600 billion by 2027 (figure 4). The rule of thumb is that for every $1 companies spend on Nvidia chips, another $1 needs to be spent on buildings for the data centres running the AI apps and peripheral equipment like cooling systems and networking infrastructure. This combination means that by 2027, roughly $1.2 trillion is likely to have been spent building the infrastructure needed for generative AI. This figure is similar in today's dollars to the amount spent on internet infrastructure in the second half of the 1990s.

Return on the investment

The question uppermost on the minds of many investors is what sort of return big tech companies will reap from this staggering investment. Indeed, the large tech firms, which account for the bulk of spending on AI, have seen the rate at which earnings are converted into free cashflow fall sharply as they have yet to see meaningful revenue from these investments.

To justify $1.2 trillion of spending, it's estimated that around $500 billion to $600 billion of revenue will need to be generated. But so far the 'monetisation' of generative AI has been lacklustre. The biggest standalone application OpenAI only has several billion in revenue; for all applications in total so far, it's a little less than $20 billion. This shortfall has led some high-profile investors to start wondering what will plug the $400 billion to $500 billion shortfall to keep the AI investing trend on track.

One answer is in the form of 'AI agents'. In September, Salesforce, a leader in cloud-based customer relationship management software, announced its vision for the future of enterprise software, which describes software systems with multiple business-wide applications. Instead of companies buying licenses for their employees to use in call centres, Salesforce would create AI agents to perform these tasks, potentially slashing wage bills for their customers.

Salesforce's off-the-shelf agents are augmented chatbots that can respond to complex queries and take actions to manage requests. An AI agent will reason and plan on the company's behalf by connecting with the corporate database. For instance, it could rebook flights for a passenger across three different cities on three different days, saving a call to a service agent. These AI agents can take advantage of large action models (LAMs) built on top of large language models (LLMs), and execute functions in other systems and applications (see box 'AI in action'). As human service agents are freed up, their roles could be expanded into sales or marketing, continuing the long-term shift of labour into tasks that add more value.

Ultimately Salesforce's new class of agents will be an important test of whether the trillion dollars spent on Nvidia chips can yield major productivity improvements. Stage one of the generative AI boom benefited the companies selling chips and hardware. In stage two, the value could shift to the providers of software and cloud services, as these models go into production. In stage three, a whole new set of applications and companies may emerge.

Benefits far and wide

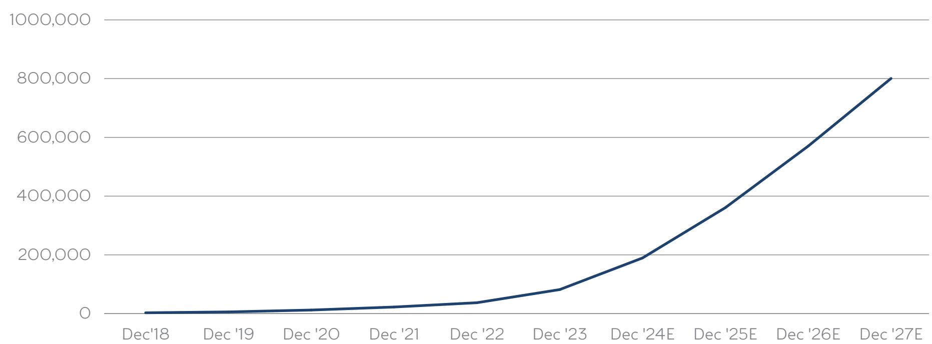
It is worth remembering that generative AI is a general-purpose technology with the potential for wide reaching benefits, affecting every industry. The greatest benefits are likely to be felt far and wide, beyond the technology sector. Every company has functions such as sales, marketing, IT, accounting and human resources with potential for significant productivity gains. With the annual global wage bill estimated at $44 trillion, there is a great deal to aim for.

It is possible that we are living through an example of Amara's Law, which states that the impact of new technologies tends to be overestimated in the short run and underestimated in the long run. Perhaps the lag in money-making applications is at least partly attributable to nervousness about the output of LLMs, particularly when trained on the open internet –

Figure 4: Chips with everything

Nvidia's cumulative sales of data-centre chips ($ millions) has been rising dramatically and is forecast to keep going up as companies invest in generative AI technologies.

Source: Factset and Rathbones



AI IN ACTION

Large language models (LLMs) are advanced AI systems trained on vast amounts of text data to understand, generate and analyse human language. They excel in natural language processing tasks such as text generation, summarisation, translation and conversation. By predicting and constructing coherent responses, LLMs serve as the foundation for various AI applications.

Building on LLMs, large action models (LAMs) extend their capabilities by integrating them with external systems and applications. LAMs are designed to not only process language but also perform tasks or 'actions' in response to user input. These actions might include executing commands, retrieving data, interacting with software or managing workflows. This enables LAMs to move beyond passive language generation and actively interface with other tools and environments to complete complex tasks.

In essence, LLMs provide the cognitive foundation for understanding and generating text, while LAMs transform this understanding into practical, real-world functionality by leveraging integrated systems. This combination opens up powerful new possibilities for both automation and problem-solving.

they can be prone to biases and hallucinations, or inaccurate information. As the models become more sophisticated, these concerns should ease. But they will also require more computing power. Semiconductor manufacturing equipment supplier ASML estimates that if the uptake of LLMs grows as expected, the computing power required to run them will increase 16-fold every two years. That is much faster than the two-fold increase every two years for past advances in computing power, suggesting demand for hardware will continue to increase. However, there are other reasons to believe that the AI spending boom can endure even without a clear way to monetise it on the horizon. Back in the 1990s, the telecom companies funded their capital expenditure with debt and many ultimately went bust as those investments soured due to overcapacity and insufficient demand. This time around, the big tech companies are flush with cash and can easily fund their investments through the substantial cashflow they continually generate.

Pascal's wager

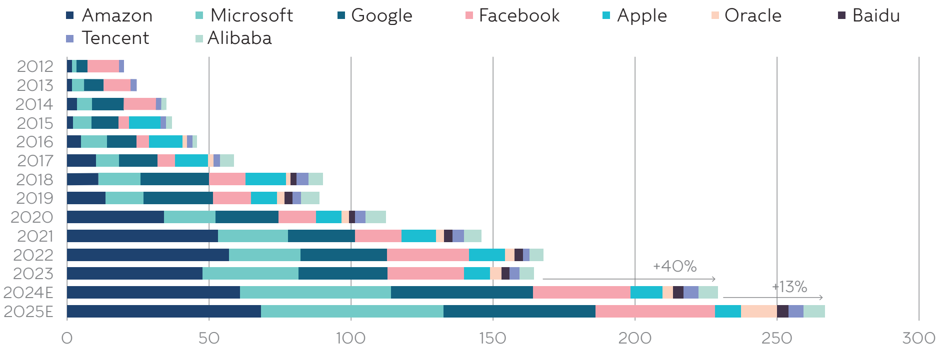
Tech companies also face a form of Pascal's wager, where AI stands in for God. In this scenario, the risk of not believing in Gen AI's potential when it turns out to be real is potentially catastrophic, while investing in it if it's a dud is relatively survivable given the deep pockets of big tech. Lastly, it could be hugely beneficial to invest significant sums today if it turns out to be as transformative as boosters claim. As Alphabet CEO Sundar Pichai put it: "The risk of underinvesting is significantly higher for us than overinvesting." This sentiment was echoed by Mark Zuckerberg, CEO of Meta, who said he would rather build AI capacity too early than too late.

The current fear of missing out being demonstrated by the big cloud-services providers could presage a pause in investment at some point over the next couple of years. But recent commentary about near-term capital spending plans suggests this is not imminent, as they have laid out roadmaps for their data centre build outs over the next two to three years that they will execute on regardless of near-term monetisation. Looking further out is hard. The two greatest threats are that either AI advancements hit a brick wall, mitigating the risk of falling behind your competitors by cutting spending on AI, or 'monetisable' uses are more limited than the market assumes. But it may take three to five years before big tech companies are convinced that there is no gold in the AI hills.

For now, to quote Citigroup CEO Chuck Prince during the 2008–09 financial crisis: "As long as the music is playing, you've got to get up and dance".

For more on developments in AI and the investment implications, see the series of articles we wrote in last year's *Investment Insights*, which you can find at www.rathbones.com/knowledge-and-insight/investment-management.

Figure 5: Big spenders
Capital expenditure (in $ billions) in the tech sector has been rising over the past decade and is forecast to jump even higher next year.
Source: Factset, Evercore ISI Research and Rathbones



LONGER-DATED BONDS MAY NOT BE AS USEFUL AS THEY ONCE WERE

In our 2024 report *Investing for the next decade*, we set out why we expect inflation to be higher and more volatile over the next decade than it was in the unusually stable 2010s. If we're correct, this situation may mean longer-dated bonds don't perform their role as a counterweight to shares as reliably as they have done in the past. Accordingly, we think it's prudent to strategically shift towards shorter-dated bonds, which offer attractive yields by the standards of the past few decades, and should be less vulnerable to inflation volatility.

In last year's report on the changing investment landscape, we argued that governments' renewed appetite for spending, widening geopolitical fractures and the increasing frequency of extreme weather events would all contribute to higher and more volatile inflation. In the period since, developments have only bolstered our case.

First, the UK's new Labour government unveiled a Budget that expanded the size of the state. This expansion was funded in part by a significant increase in borrowing, which the Office for Budget Responsibility called "one of the largest fiscal loosenings" at a Budget in recent decades.

Second, Donald Trump emerged victorious in the US presidential election. While the US has continued down a protectionist path under Joe Biden, it is likely to accelerate if Trump enacts his campaign pledges to implement universal import tariffs of 10–20%, and much higher levies on China. Both the tariffs themselves and the breakup of some globalised supply chains that might occur as a result could put some upward pressure on inflation.

Climate and commodities

Third, the prices of some more foodstuffs have surged, at least in part due to more frequent weather disruption caused by climate change. In the past few months, we've seen a renewed spike in the price of cocoa and a leap in wholesale coffee prices. That's on top of the ongoing disruption to olive oil production from high temperatures. Most recently, global wine production has slumped to the lowest level since 1961, with vineyards citing extreme weather.

One way we're adapting to this changed landscape is through the way we invest in bonds. In recent decades, these investments have performed a useful role in portfolios thanks to their negative correlation with shares. In other words, when shares fell, bonds tended to rise, acting as ballast to smooth out returns. This pattern occurred because negative shocks to the economy that hurt shares usually coincided with expectations for lower interest rates, which generally mean higher prices for bonds, whose fixed interest payments become more attractive. Longer-dated bonds, which are more sensitive to changes in interest rates, performed this function particularly well. As a bonus, they generally offered higher yields than their shorter-dated counterparts at the same time.

A necessary condition for this relationship was low and stable inflation. When inflation is low, central banks can cut interest rates to support the economy when it struggles, to the benefit of bonds. However, when inflation is higher, they are forced to hike interest rates to reduce overall demand for goods and services, thereby curbing pressure on prices. This tends to be negative for both stocks and bonds, creating a positive correlation between them. We've seen this happen recently when inflation spiked, prompting stocks and bonds to sell off together in 2022.

Adapting to higher inflation

Figure 6 shows how the relationship between stocks and bonds has evolved over time in the UK. Specifically, it shows the correlation between the monthly returns of UK gilts and the UK stock market over a rolling three-year period. When the correlation is below zero, stocks and bonds move in opposite directions. Above zero, they move in the same direction. Note how the correlation was positive during the high inflation of the 1970s and 1980s, before turning negative in the 2000s and 2010s when inflation was low, and then moving back above zero over the past few years.

The key takeaway is that in a world of higher and more volatile inflation we anticipate over the next decade, we don't expect the correlation between stocks and bonds to be as reliably negative as it has been in recent decades. In other words, we think there is a greater chance that when stocks fall, bonds will too.

In response, we believe a strategic shift towards holding shorter-dated bonds makes sense, given they are less sensitive to changes in inflation and interest rates than their longer-dated cousins. While this does mean slightly lower returns if inflation and interest rates fall, the flipside is that it should limit the hit to portfolios if high inflation causes bonds and stocks to sell off together again. As explained above, we think this is becoming more likely. Meanwhile, yields on longer-dated bonds are no longer much higher than on shorter-dated ones, as they were in the 2010s. So we won't be missing out on much by avoiding the added risk of holding longer-dated bonds.

Further reading

Find out more about the challenges and opportunities ahead in our report *Investing for the next decade* at www.rathbones.com/investment-management/investing-for-the-next-decade

Figure 6: An evolving relationship
This chart shows the three-year trailing correlation between UK shares and government bonds. We expect the relationship to be positive over the next decade, which has implications for the way we construct and manage diversified portfolios.
Source: LSEG and Rathbones

THE THEME OF SUSTAINABLE INVESTING MIGHT GET TRUMPED

Since Donald Trump's re-election, coming just days before annual climate negotiations began at COP29 in Baku, much has been said and written about what impact the result is likely to have on global efforts to tackle climate change. As Trump prepares to take office again on 20 January, we expect some hostility not only to environmental policy, but also on social and governance issues of relevance to investors – in other words, across the spectrum of ESG.

We believe Trump's re-election deals a serious blow to global ambitions to tackle climate change. However, the consensus among experts is that policymakers are better prepared this time around and there are fewer unknowns than there were at the start of Trump's last term eight years ago.

The US wasn't able to withdraw formally from the 2015 Paris Agreement– which aims to limit global temperature increases to 1.5°C – until the end of Trump's first term in office. This was because countries could only give notice to three years after it was adopted. However, there will be no such obstacle this time round, with Trump pledging to pull the US out of the agreement immediately after taking office.

The President-elect is also expected to take aim at climate-friendly policies implemented under Biden's Inflation Reduction Act (IRA), which he referred to as the "green new scam" during a campaign rally. As we noted in our pre-election report *Polls Apart*, with spending for clean power initiatives from the IRA benefiting Republican states disproportionately, there may be limits to how far Trump's government can go in reversing all of the renewable energy funding that is in train.

Furthermore, with the US stepping back from its leadership role on global climate action, there could be an opportunity for countries and businesses – notably in China and European economies – to not only fill the void, but also to steal a march in the green transition race.

Shifting sands

It's not just the environmental policies of the previous administration that are expected to be reversed or scrapped under the new government. Trump's deregulatory agenda could have profound implications for shopfloor workers and corporate governance in the US.

> **Major changes are afoot that are likely to alter the dynamics of ESG investing in the US significantly**

Messages have been mixed about the extent to which the new Trump administration will be pro-worker or pro-management. On the one hand, conservative policymakers close to Trump have been discussing measures to take away overtime pay, repeal workplace health and safety regulations, and change child labour laws to allow teenagers to work in 'hazardous' occupations without parental consent. A number of blue-chip American companies have also been abandoning initiatives aimed at fostering diversity and inclusivity at their workplaces in anticipation of a greater threat from legal challenges.

On the other hand, Trump has recently expressed an openness to raising the federal minimum wage. He also announced his intention to nominate Oregon's pro-union Representative Lori Chavez-DeRemer for Secretary of Labor. This move has drawn support not just from the unions, but also from progressive members of Congress.

Shareholder power

Investors have the ability to press publicly listed US companies to implement changes or ask them to disclose information that might help shareholders to make better-informed investment decisions. One way is by putting forward shareholder proposals for a vote at annual general meetings (AGMs). They are an important tool at the disposal of investors to increase corporate transparency and hold companies to account for poor decision-making or corporate malpractice.

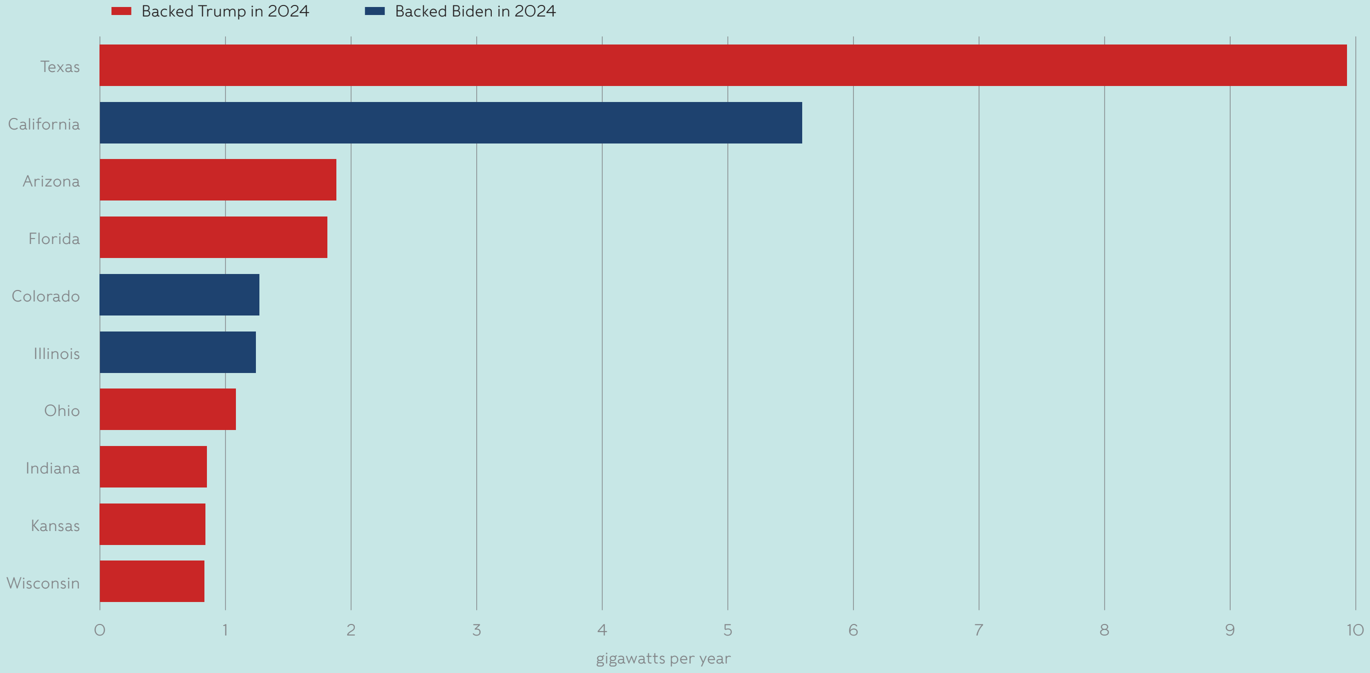
However, Trump is expected to sanction sweeping changes to the leadership of the US financial regulator, the Securities Exchange Commission (SEC), which has the power to block or approve shareholder proposals from being put to a vote. This could well mean that investors will have a tougher time using shareholder proposals to express concerns or discontent over the running of a company.

Major changes are afoot that are likely to alter the dynamics of ESG investing in the US significantly. It becomes more important than ever that we leverage the relationships we have built with American companies to ensure corporate sustainability remains high on their agendas.

Further reading

Find out more about the potential implications of Trump's policies in our special report *Polls Apart* by visiting our online Election Hub at www.rathbones.com/rathbones-election-hub-financial-insights-2024-elections

Figure 7: Clean power installations in the top 10 US states in 2023
Funding for clean power following the Inflation Reduction Act has disproportionately benefited Republican states.
Source: American Clean Power; according to 2024 presidential election



FINANCIAL MARKETS

The final quarter of 2024 was shaped by diverging growth patterns, shifting monetary policies, and geopolitical tensions. The US economy sustained steady growth, supported by resilient consumer spending and a recovery in industrial production. In Europe, Germany entered a technical recession as weak exports and manufacturing output weighed on its economy. Meanwhile, the UK faced subdued growth and a rise in inflation, adding to its challenges.

The US Federal Reserve (Fed), European Central Bank and Bank of England all cut interest rates during the quarter to help support their economies. In many regions growth concerns took precedence over inflation worries. However, expectations for further interest-rate cuts were scaled back as policymakers sought to balance stimulating growth with the ongoing need to tame inflation.

A volatile period

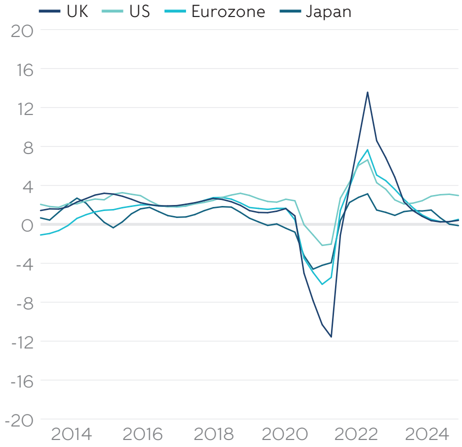
The quarter started on a positive note, with gains in the tech sector and upbeat economic data lifting Wall Street. US stocks soared to new highs following Donald Trump's election victory, despite his threats to implement sweeping tariffs.

US Treasury yields spiked in November, marking one of the sharpest sell-offs in five years (pushing yield higher) as markets anticipated that Trump's policies might drive inflation up, before recovering some losses into the end of the year. Higher government bond yields globally and reduced expectations for further Fed rate cuts added to market uncertainty heading into 2025.

The rise in geopolitical tensions fuelled demand for the perceived safety of gold, which surged to an all-time high in November. Meanwhile, oil prices fell below $70 a barrel as OPEC+ members agreed to delay planned crude production increases, reflecting concerns about weak demand amid global economic weakness.

GDP growth

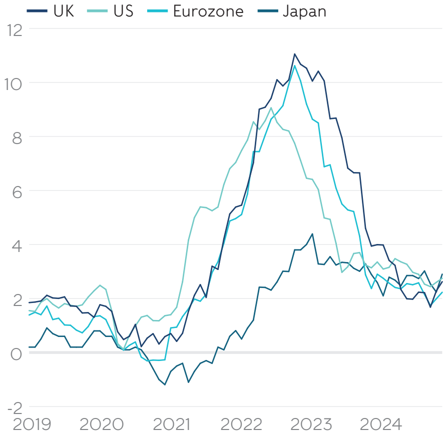
Annual change (%)



Source: Factset and Rathbones

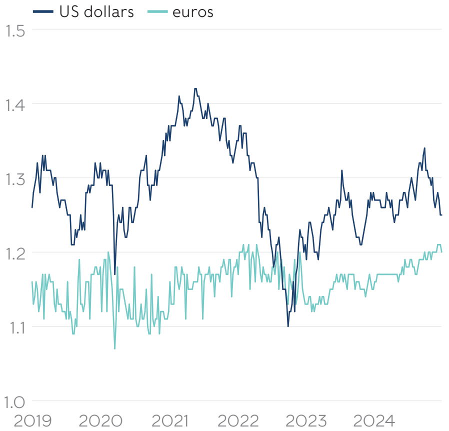
Inflation

Annual change (%)



Source: Factset and Rathbones

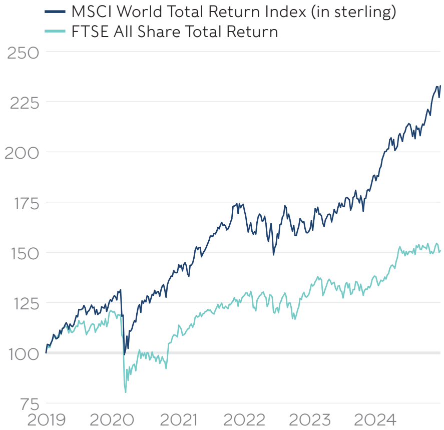
Sterling



Source: Factset and Rathbones

Equities

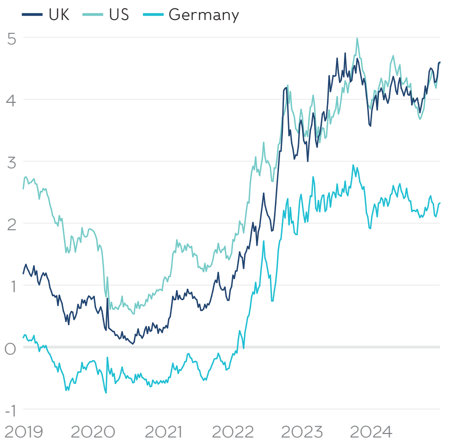
December 2018 = 100



Source: Factset and Rathbones

Government bonds

10-year yields (%)



Source: Factset and Rathbones

Gold

US dollars per troy ounce

Source: Factset and Rathbones

The value of investments and the income from them may go down as well as up and you may not get back your original investment. Past performance is not a reliable indicator of future performance.

ADDITIONAL INFORMATION

Information valid at 31 December 2024, unless otherwise indicated. This document and the information within it does not constitute investment research or a research recommendation. The value of investments and the income generated by them can go down as well as up.

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