

## Transcript

### Financial Market Commentary – Review of 3rd Quarter 2025 and Outlook

#### Simon Lewis on 21 October 2025

Hello and thank you for joining our latest financial market commentary. Last time, I talked about how investment volatility had defined the first half of the year, brought about largely by the uncertainty (or havoc) created by President Trump's economic policies. I also said that we were nevertheless cautiously optimistic about the outlook for global financial markets for the remainder of the year.

That optimism was vindicated in the third quarter of the year, with PMW portfolios performing well. This chart shows the underlying investment performance of a PMW Balanced portfolio during the period. Of course, it followed a very volatile first half, after which portfolios were broadly even. So, the strong performance of the third quarter needs to be amortised over the year to the end of September. But it's nevertheless a respectable outcome in both nominal and real terms. And over periods of one and two years, we can see that investors have been rewarded for the volatility that has been tolerated.

So, what does the future hold?

You might have noticed that a lot of financial commentators are talking about the risk of a financial market crash.

How worried should we be?

I've seen some articles draw parallels with the stock market of 1929, but the stock market crashed in 1929 because of the Great Depression. There's no sign of a recession in the US economy, let alone a depression. So, in our view, such comparisons are meaningless.

And this chart, recently produced by the US Federal Reserve, shows that corporate and household debt in the US is relatively low and trending down, so comparison with the financial market crash of 2008 is also wide of the mark.

To form an objective view, it's important to understand the role and motivation of financial journalists. There's an old media saying, "if it bleeds, it leads".

Readers like scary stories more than happy ones. Journalists are therefore inclined to give customers what they want, which is fine so long as they are guided by integrity and intelligence while doing so.

A Financial Times journalist recently wrote:

"Murmuring darkly about how we are all in big trouble makes one look and feel clever. I don't know why this is so, but pessimism and insight are not the same thing. Scepticism is part of a journalist's job. Scepticism is a tool; pessimism is a bias."

The reality is that financial market highs are most often followed by new highs. And it's probably true that far more money has been lost by investors preparing for corrections or trying to anticipate corrections than has been lost in corrections themselves.

At PMW we make portfolio adjustments to reflect the prevailing macro-economic environment and the secular headwinds and tailwinds that will likely impact the value of assets in the future. Over time, that approach has worked well, and we see no reason why it won't work well in the future.

Let's have a look at the factors that are likely to prove positive for financial markets.

You might have read about the recent spat between the US and China about rare earth elements. Rare earth elements aren't that rare. In fact, they are naturally abundant. It's simply that in recent decades, it is predominantly China that has been prepared to live with the environmental damage caused by their extraction and processing. For China they are now a useful bargaining chip with the US, which needs rare earth elements to continue the current pace of technological development.

But that leverage is likely to reduce over the next decade as extraction and processing is stepped up in other parts of the world, notably Australia and Canada.

If the western world sets a price floor for such elements, it is likely to accelerate the reduction in reliance upon China. So, China will be keen to use its advantage now, to extract better terms for tariffs. Which means that this issue might not become a geopolitical problem, and financial markets can move on to considering other risks.

At the moment, US financial markets are largely driven by the eye-watering level of investment in AI by a handful of large US technology titans. More recently, such investment has accounted for almost 40% of the growth in US GDP.

Is it a bubble? Not necessarily.

This is nothing like the dotcom bubble at the turn of the century. Back then, companies with no revenue and no proven business model were speculatively valued in their billions. This time the main protagonists are valued in their trillions, but they have a proven business model and are already generating many billions in revenue. For example, NVIDIA, which makes GPUs for AI applications, is forecast to generate revenue of \$130 billion this year. And it is predominantly the profit on such revenue that is being invested in expanding their AI capacity.

Although investment levels are high, that money is being invested in something that is almost certain to have an enduring value – data centres, computing power and energy supply.

The US now owns about 75% of the world's AI supercomputers, China has about 15%, with the remaining 10% distributed elsewhere. For example, the UK holds around 3% of world compute capacity.

The UK Government has stated its intention to treble its compute capacity by 2023 but to put that in context, the increase is less than a single data centre project currently underway in the US by Meta Platforms, the owner of Facebook, Instagram and WhatsApp.

But data centres need a lot of power, which explains why Microsoft has recently purchased all the electricity that will be produced over the next 20 years by Three Mile Island, the infamous US nuclear power station.

There are countless other examples of investment on a spectacular scale. It might be overdone, but it's not going to turn to dust.

What else does the US have going for it? For those of us who are a bit nerdy about economics, the Levy-Kalecki Profit Equation succinctly defines the relationship between US corporate profits, corporate investment, household savings and government deficits.

In summary, both higher corporate investment (by which I mean acquiring an asset) and higher government deficits (government borrowing to spend) the higher we should expect aggregate corporate profits to be. The US currently has a large fiscal deficit, and the current policy pathway does not suggest this will soon change. So higher corporate profitability should be expected. Sadly, it's not a theory that works so well for the UK economy, which has a much bigger public sector component.

Other tailwinds include the momentum now established for US interest rates to fall. Unlike the Bank of England, the US Federal Reserve has a dual mandate. It must both control inflation and maintain employment and its concerns for the latter are likely to encourage further rate cuts. That will be good for global financial markets.

We've spent a lot of time talking about the US so let's turn to the domestic scene. Financial considerations in the UK are now dominated by speculation in the run up to the Budget. Rachel Reeves has the impossible task of satisfying bond markets, Labour bank benchers and the electorate. In that order of importance.

Bond markets are already rattled by the lack of Government progress on reigning back spending. And this chart shows that the Government can no longer depend on pension schemes to Hoover up its debt. Mark Carney, whilst Bank of England Governor famously said the UK relied upon the kindness of strangers. And the less happy they are, the greater the rate of interest they will demand for their financing.

The current UK Government ideology seems to be neatly summed up by an old Ronald Reagan quote. He was summarising his view of the economic policies that prevailed before he was elected US President.

If it moves, tax it.

If it keeps moving, regulate it.

If it stops moving, subsidise it.

With the Government seemingly incapable of meaningful spending reductions and apparently unwilling to break (the letter if not the spirit) of its manifesto pledges, 'broad-shouldered' people are becoming an endangered species in the UK.

We should brace ourselves for a reduction in tax relief for pension contributions by high earners new taxes on higher value properties, an extension of the national insurance regime to cover some unearned income and a broadening of the remit for VAT and a further tightening of the inheritance tax net.

As far as the future investment outlook is concerned, we think it's important to anticipate Trump policy decisions by understanding what's important to both him and those that back him. Asset allocation decisions should then be aligned with such interests.

I hope that this update has been useful, and I look forward to catching up with you at the end of the year.

In the meantime, I hope that you find something to smile about....

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