

The Right Bill of Lading

‘...Antonio hath a ship of rich lading wrack’d on the narrow seas;’
(*The Merchant of Venice, Act III, Scene I*).

I invite you to cast your minds back to a now-historical acronym, the poster-child of financial repression otherwise known as ‘Zero Interest Rate Policy’ (ZIRP), which represented a decade-long drag on savers’ returns caused by the asymmetric monetary policies of central banks in the wake of the Great Financial Crisis of 2007-9. In its wake, we referred to the bond market as ‘return free risk’ and scoffed at the typical 60/40 model strategy adopted by ‘balanced’ portfolio acolytes since time immemorial, as real returns remained decidedly in the red. Higher yielding (and sometimes inflation-friendly) equity alternatives were all the rage. Rather than Tom Wolfe’s ‘Master of the Universe’ an ill-fated bond trader who headlined ‘The Bonfire of the Vanities’ in 1987, being employed as a fixed income specialist in the late 2000s was more akin to Michael Lewis’ exiled manager of ‘equities in Dallas’ from his 1989 book, ‘Liar’s Poker’.

And yet, as Paul Crocker reminds us from his ‘painful experiences’ later in this Briefing, to focus entirely on the equity bucket to achieve a real return on cash after inflation was somewhat of an anomaly, albeit one which lasted more than a decade, bond markets further dogged in the 2020s by the rampant inflation of the post-pandemic era. At that exact point, I was almost surprised that Time Magazine failed to headline the demise of the bond market in the manner of their famously mistimed 1966 cover, but instead of ‘God’, asking: ‘Are Bonds Dead?’ Like pulling a large splinter from one’s thumb, the gradual narrowing of the yield gap between equities and bonds and a return to historically normal interest rates, thereby removing equities as a one-way street for investment, has been a painful experience since this process started in late 2021, but it now leaves us in a place where we can better manage risk-adjusted returns. A ‘balanced’ portfolio is now truly diversified. With the exception of precious metals, maintaining key differentiators (cash and sovereign debt) no longer comes at the expense of real capital erosion, now generating a return after inflation which is visible without the assistance of a microscope.

Equity markets usually fret over ‘inverted’ yield curves, where borrowing costs are lower over the long-term, suggesting that lower economic growth, requiring looser fiscal/monetary policies are in the pipeline. More recently, however, sovereign yields at the longer end have been pushed higher by the ‘term premium’ (an additional reward offered to those brave borrowers of government debt). With Reform UK waiting in Labour’s already depleted Treasury ante-room, Europe searching for pennies behind the sofa to fund EDIP*, Japan grappling with higher debt interest payments and Donald Trump not playing three-dimensional chess but rather ‘eating the pieces’ (as one former official recently put it) with TACO† sauce and a side-dish of un-presidential ‘F’ bombs, the fiscal probity of governments has deteriorated, blowing away confidence in long bonds, like chaff in the wind. While banks might celebrate their improved interest margins on a rising yield curve, and depositors cling on to higher than expected interest rates while they last, this is not good news for penurious governments, busy financing increased spending on their defence/healthcare/education budgets (delete as appropriate). Combined with concerns over ‘sticky’ inflation (driven by services sector cost increases in the UK and a weaker dollar/ higher post-tariff prices in the US), this has gone down like a lead balloon in recent longer-dated Treasury and

gilt auctions. Reluctance to put your money where Trump’s mouth is, is certainly evident from second quarter 2025 fund flows out of longer-dated US bond funds (-\$11bn), shifting into their short dated equivalents (+\$39bn).

If one remains concerned over Trump’s chess-playing abilities, the UK’s political largesse, Japan’s interest bill and/or Europe’s expensive neighbourhood watch scheme, but still seeks a fixed income allocation as part of a healthy and diversified portfolio, where does this leave corporate bonds? Credit ‘spreads’ (the difference between yields on sovereign and corporate bonds of similar maturities and coupons) are currently slim, indicating that there is scant reward on offer to corporate creditors (at the mercy of shareholders and market sentiment) as opposed to tapping up a sovereign entity (which can print its own money and set taxes). Higher-yielding bonds come with commensurate risk however this can be partially mitigated by investing in specialist ‘short duration’ bond funds, which are (usually) highly diversified with low default rates (and a smaller window of opportunity for economic or monetary vicissitudes). These short-dated funds also have a lower sensitivity to interest rate fluctuations as their underlying bond prices ‘pull to par’. While representing higher duration risk (certainly if one buys a passive exchange traded fund), there is also the prospect of achieving a positive real return on inflation-linked securities for the first time in what seems like an eon.

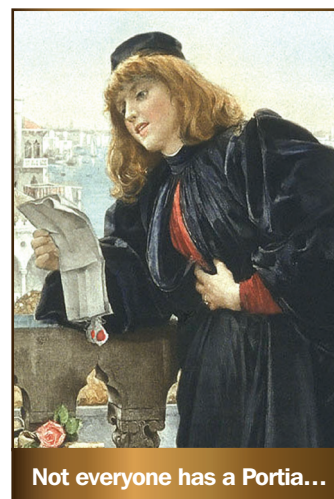
Therefore, even with a ‘stagflation light’ global economic outlook on the horizon which would make Marx gusts seem like mere zephyrs, it is possible to strengthen one’s umbrella with some fine-tuning at the shorter-end of the corporate and sovereign yield curves, as a buffer for unexpected and unwelcome near-term volatility. Furthermore, the return of fixed income investments to the asset allocation table has been largely welcomed by prudent investment managers following an era of monetary atrophy and uncomfortable correlation. The Venetian merchant, Antonio, did not think that all his ships could sink at once but he nevertheless lost his vessel of ‘rich lading...on the narrow seas’ of Goodwin Sands. Watching your investments rise and fall does not necessarily equate to life and death or pounds of flesh, but it can still be a very painful experience if not suitably diversified, sometimes leading to snap decisions; often comforting and often wrong. Not everyone has a wily Portia at their side to unwind a bad contract.

Mary Tait

CHIEF INVESTMENT OFFICER - JULY 2025

*The European Defence Industrial Programme

†See Pieter Cloete’s article!



Not everyone has a Portia...

Perilous Waters

Frustration, despair and hope are three nouns which investment managers have heard frequently in recent months. To paraphrase Peter Benchley, the film of whose famous novel, *Jaws*, has just celebrated its 50th anniversary: when will it be safe to go back into the water?

At no time in recent history have markets been asked to discount the sheer number of moving parts currently flying around. Many, but not all, can be attributed to US President Donald Trump whose bombastic style of leadership contrasts crudely with the measured diplomacy usually associated with a leader of a major western democracy. Markets eschew uncertainty but they have had it in bucketloads since Trump was inaugurated last year.

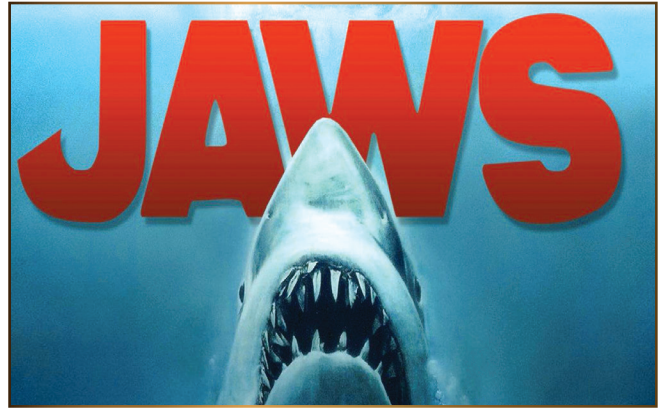
The first 100 days of Trump 2.0 was as tumultuous as they come. A superfluity of contradictions, arguments, garbled threats and bluster all spewed out on social media or via the President's venomous press secretary. The crowning glory of 'Liberation Day', which applied an infantile level of mathematics to the complexity of global trade tariffs, primed equity markets for a series of stomach-churning ups and downs. Add Ukraine, Russia, Gaza, Israel and now Iran into the mix and the phrase 'investor fatigue' doesn't quite cut it. Frankly, it has been exhausting.

Counter-intuitively, relatively narrow equity and bond market performances have disguised much of this trauma. But the US Dollar has been a casualty. Because America comprises such a large slice of global equity allocation, returns in other major currencies, such as sterling, have been affected. By way of example, in US Dollars, global equities have gained by around 4.5% over the first half of 2025. In sterling terms, those same equities are down by nearly 3%. The credit rating agency, Moody's, summed up investor mood very well, by downgrading US sovereign debt by a notch to Aa1 earlier this year. Not exactly the financial panacea painted by MAGA aficionados.

But despite the shaky backdrop, all-important corporate results have generally held up well so far this year. The impact of tariffs has yet to bite meaningfully whilst the technology sector has been buoyed by fast-moving artificial intelligence developments.

Investors have, however, become far more particular about valuation. Based on 2026 consensus earnings, 'AI' cheerleader, **Nvidia's** share price touched an almost analogue 30x price/earnings ratio earlier this quarter. In the rarified operating environment of 'AI', this is almost cheap. On the other hand, **Tesla** now trades on an equivalent multiple of 174x earnings, the shares pinned down by cheap Chinese electric cars and a Marmite CEO. That P/E ratio is taking an awful lot on trust.

No surprise then, that the respective share prices of these two



high profile Magnificent 7 constituents have moved in opposite directions this year. But the focus on valuation is, we think, a healthy one and also explains, in part, the outperformance of lowly rated markets in Europe and UK. But don't get too excited. Whilst companies can, in the near-term, sidestep a weak operating environment, they cannot defy gravity forever. Economic growth in Europe is forecast to be flat for the foreseeable future, increased defence budgets notwithstanding (more debt?). And whilst global growth is slowing almost everywhere else too, it does at least remain positive in America. Investors, though, still need to pay up for the privilege of owning US equities. In a world of Trump madness, tariffs and tax threats, that is not always an easy decision to make.

Mary writes elsewhere in this newsletter about bonds. When interest rates were at rock bottom, the fixed interest market offered scant rewards to investors but significant benefits to issuers who could borrow long-term money at rock bottom prices. Whilst bonds are not immune to volatility, they provide a useful source of stability to balance out their more excitable equity cousins. Their 'Achilles' heel' is inflation (which is very much alive and kicking). Inflation destroys fixed returns in real terms and explains why we prefer quality equities as more reliable long-term guardians of capital.

Equity outperformance might seem like a distant prospect, but it is worth reminding weary investors (especially those who have yet to experience a proper bull market) that over almost every meaningful time-period during the last 100 years, equities have outperformed all other asset classes. Over the last 5 years (admittedly an extreme example, given that this period spans COVID), global equities rose by 9.6% annually, versus a fall of 4.6% in global bond markets. Much of this outperformance will have taken place over a relatively short period of time and at the most unexpected of moments (which is why clever trading strategies often fail dismally). As ever, the advice is to stay invested. But like many things in life, balance is the watchword, especially when the world seems to be more unpredictable than ever.

Russell Collister

Novelisation Correlation: Turning The Page On Traditional Portfolios

My wife and I love nothing more than to unwind with a good TV show. Between work, family life, and exercise, finding downtime isn't always easy. That's why a short, sharp episode of a great series is always welcome. We've watched many over the years, but my favourite remains 'The Big Bang Theory'. In fact, I borrowed the title 'Novelisation Correlation' from 'The Big Bang Theory', Season 11, Episode 15. The term 'correlation' in that episode cleverly plays on the connections between fiction and reality – particularly how one character's novel mirrors real-life relationships.

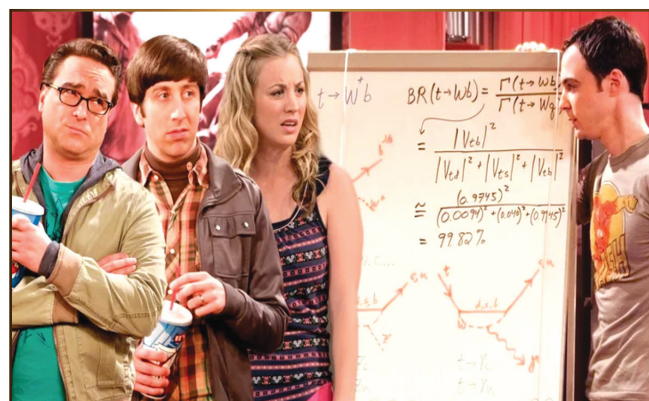
In the investment world, we also talk a lot about correlation – specifically, how different asset classes behave in relation to one another. The goal is to find assets that respond differently under various market conditions, helping to reduce overall volatility and improve risk-adjusted returns. For instance, when stocks fall, bond prices may rise, providing a stabilising effect. Interestingly, Penny – one of the show's main characters – mentions having a diversified portfolio of stocks and bonds, a surprisingly savvy move for her character.

But a word of caution: correlation does not imply causation. Just because people eat more ice cream on hot days doesn't mean ice cream causes the heat. Similarly, seeing firemen at a fire doesn't mean they caused it. Misinterpreting correlation can lead to poor investment decisions.

Historically, the low (or even negative) correlation between stocks and bonds gave rise to the classic 60/40 portfolio—60% stocks, 40% bonds. This model worked well pre-global financial crisis, but less so in the years that followed. During the long period of low bond yields, the phrase 'TINA' (There Is No Alternative) became popular, reflecting investors' reluctance to hold bonds. Today, with bond yields more attractive, 'TINA' has faded, replaced by phrases like 'TACO' (Trump Always Chickens Out), referencing policy reversals such as softened Chinese tariffs.

But what about assets outside the traditional stock-and-bond framework? These are known as 'alternative investments'. Why consider them? Because they offer diversification, often behave differently from traditional assets, and can reduce portfolio volatility. Ultimately, they aim to deliver better risk-adjusted returns. Take gold, for example. We hold it widely for clients, primarily through the iShares Physical Gold ETC. This year, both stock and bond markets have been volatile, with dislocations across countries, sectors, and investment styles. Long-dated U.S. bonds in particular, have struggled due to fiscal uncertainty under the current administration. Traditionally, the U.S. dollar served as a safe haven, cushioning declines in U.S. assets. But recent geopolitical tensions and the weaponisation of the dollar – especially post-Ukraine war – have led investors to question the long-term dominance of U.S. markets and currency. In this environment, gold has flourished, delivering double-digit returns. Its appeal lies in its scarcity, its role as a store of value, and practical uses in jewellery, electronics, and industry.

Bitcoin shares many of gold's attributes. It's scarce, acts as a store of value, and has growing utility. Around 2 billion people globally remain unbanked, yet 1.5 billion of them have access to mobile phones and the internet. In developed markets, Bitcoin is often



seen as a long-term store of value. In developing and frontier markets, it's increasingly used for its fintech utility. Despite its volatility, Bitcoin has advantages over gold: it's more divisible, easier to store and transfer, and even more scarce due to its capped supply and diminishing issuance. Unsurprisingly, Bitcoin has performed strongly – especially since BlackRock launched the world's first spot-backed iShares Bitcoin Trust ETF. I believe we've witnessed Bitcoin's evolution into a legitimate asset class, particularly after the U.S. officially recognised it as a strategic reserve asset. President Trump's executive order, 'Establishment of the Strategic Bitcoin Reserve and United States Digital Asset Stockpile', marked a turning point. Not only is Bitcoin now held at the federal level, but several U.S. states are following suit. Whilst I wouldn't recommend taking investment advice from a sitcom, it's amusing that 'The Big Bang Theory' mentioned Bitcoin as early as 2017 – once again ahead of its time.

Of course, you don't need to invest in gold or Bitcoin to access alternative assets. Real estate is another option, and we invest widely into the likes of Prologis, Equinix and Segro. Many people already have exposure through home ownership, which is also a form of private equity, and we too invest widely in private equity through structures offered by HarbourVest and Pantheon. Infrastructure is another key alternative asset class, and we hold positions in funds such as Russell OpenWorld and the Ecofin Global Utilities and Infrastructure Trust. Until recently, low interest rates favoured capital-light, growth-oriented industries. But with rates now higher and infrastructure underfunded for years, this sector looks attractive – especially if income and value strategies remain in vogue.

One of my favourite alternative holdings is the Trojan O Fund, which we include in client portfolios. While it may deliver modest returns during calm markets, its performance tends to shine during periods of market stress, thanks to its flexible mandate and resilient underlying assets.

In today's complex and volatile financial landscape, alternative investments offer clients a powerful way to diversify, build resilience, and enhance long-term returns. By stepping beyond traditional assets, investors can access opportunities that are less correlated with public markets, hedge against inflation, and align with their strategic goals. Alternative assets are no longer niche – they're essential tools for building a robust, future-ready portfolio.

Pieter Cloete

SENIOR INVESTMENT MANAGER

My Rules For Investing

Seeking 33A Melville Street in Edinburgh, Eric Morecambe's quote: 'I am playing all the right notes – but not necessarily in the right order' came to mind, because I was looking for the Library of Mistakes in the twilight of my career. This is a free-for-all library dedicated to the study of financial history, combining educational courses, podcasts and events programmes. Founded by Professor Russell Napier, who hosts many of the events, it's based in a city founded by financial services and whose forefathers included Adam Smith, the economist and philosopher.

The first time my 'notes were in the wrong order' occurred within days of my career starting as a trainee stockbroker. A former founder of the company called into the office to execute a few trades and introduced himself by saying: 'people normally finish their careers in Dorset, not start there'. I did wonder if my career was doomed, by failing to appreciate the importance of etiquette; wearing a grey pinstripe suit and white shirt, even in rural Dorset where many clients' attires on market days were wellies and waterproof over-trousers, wandering into the office with a bundle of cash after selling some livestock. Much has changed in those intervening years. For starters, jobs were rarely advertised - it was all about who you knew. As I knew no-one, I wrote 140 letters to every stockbroker in the country. Training started in the back office and if all went well, you were invited to the front office. You needed to pass tests and interviews, all based in London, just to be able to place a deal over the phone, not forgetting to say 'sir' after every second word. Failure to respect seniors was serious and could result in being reported to your employer's senior partner, or worse, being barred from trading. To trade on the floor of the Stock Exchange you needed to pass your Stock Exchange exams, but even having achieved these you could still possibly fail the Membership interview. Even when all of this was completed, you still had to buy a share in the Exchange, and it was not cheap. The library was packed with books reminding us of this fascinating past and the sector continues to evolve, but I would be lying if I said I did not miss these early days.

The library's name truly resonates, given that mistakes are repeated by different generations of investors, politicians and central bankers. In other industries, lessons are learnt from previous failures, but regrettably this does not apply to the world of politics, economics and investing. Only timeframes differ. Sectors and stocks rotate from most-favoured to most-hated, valuation multiples expand and contract, interest rates rise, then fall and in all speculative cycles new investors get sucked in and ejected with just a token amount of their initial investment. However, it is these painful experiences which form subconscious rules to dominate a thought process and perhaps it's time to share some of my personal ones, because I have certainly made my share of bad calls over the years and they hurt. So here we go:

1. Don't dig too deeply analysing an opportunity. Getting stuck in financials risks overlooking qualitative and emotional factors. Also don't ignore the impact of longer-term demographics.
2. Build and reduce positions gradually. On shocking news, ask yourself if it's a buying opportunity. If the answer is no, sell.
3. Analyse a share as if you are thinking of buying the entire company.



4. Always distinguish between investment and a speculation.
5. A growing income stream provides options when circumstances change (and change they do).
6. The three drivers of return are: quality, value and momentum. When building a position, it's the former two which are most important (valuation multiple expansion drives returns) and the latter when starting to exit.
7. A low valuation at the time of purchase improves the prospect of improved longer-term returns. (Taking data from 1927, a Schiller P/E of under 7x at the time of purchase would (on average) deliver annualised returns of 10.8% over ten years. Pay over 28x and this falls to -0.5% per annum).
8. Momentum applies to all assets. It's a powerful force which can be both positive and negative.
9. Don't ignore your base market/currency.
10. In drawdown, to reduce the risk of a negative spiral during market turmoil, don't underestimate the importance of a decent proportion of withdrawals coming from income streams, remaining truly diversified.
11. Over-diversification provides a false sense of security. Simplistically, there is cash, quality sovereign debt, gold and then almost everything else falls into the same bucket, although there will always be exceptions (depending upon what is driving a collapse in confidence).
12. Modest and controlled leverage is a return enhancer, but ultimately debt causes problems, and interest rates are not easy to control. Governments can print money, and corporates can't but it's bond vigilantes who ultimately dictate interest rates in a crisis.
13. Don't panic in a market collapse, use the volatility to your advantage and buy/switch to better quality.
14. Over time, everything mean-reverts, so be wary of the comment 'it's different this time'. It never will be until humans can control their emotions.
15. You must take risk to protect capital in real terms; therefore, a longer-term time horizon is vital. (Over 100 years of US market data, around 40% of the time investors lose money relative to inflation over a month. Expand the time horizon to 20 years and there has been a 100% success rate). If you are interested in the short term, go racing: There you'll find a guaranteed winner.

Paul Crocker

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The investment team at FIM Capital Limited hopes that you have enjoyed reading our articles this quarter. If you are not currently receiving our Investment Briefing on a regular basis but would like to do so in future, or you wish to inform us of a change in your contact details, please contact us at enquiries@fim.co.im. Equally, please contact us if you no longer wish to receive our Briefing and we will remove you from our mailing list.

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