THORNTONS INVESTMENTS

Markets Review - to end June 2025.

THORNTONS WEALTH

Market Returns

(Returns in £)	1 month	3 months	6 months	1 year
UK Equities	0.3%	3.2%	6.8%	7.2%
Global Equities	2.9%	5.1%	-0.4%	5.7%
UK Gilts	1.3%	-0.2%	0.3%	-2.5%
UK Property	0.3%	1.5%	3.0%	5.3%
Gold	-1.6%	-1.0%	14.3%	30.2%
Commodities	1.1%	-8.5%	-6.5%	-1.2%
Sterling	0.1%	1.4%	2.0%	3.4%

Returns to 30th June 2025. Source: Refinitiv

Market Overview

One might be forgiven for thinking that financial markets had failed to read any news headlines during the first half of the year, with most stock markets finishing at or close to record highs. Wars, tariffs and threats to institutions that have underpinned prosperity in the West since the Second World War, appeared to have been shrugged off. However, beneath the top line there has been a great deal of volatility. The US dollar has had its weakest start since the 1970s, Chinese tech stocks have outperformed US tech, gold has soared and European defence companies are up nearly 60%.

The markets' shock at tariffs announced on President Trump's Liberation Day, have eased as they have become less frightening, with some initial trade deals (helpful for the UK) and an assumption that globally tariffs will likely settle around a 10% level. European stocks, which have been the strongest performers so far this year, have benefitted from interest rate cuts by the ECB and a willingness to increase spending by Germany. However, this will put pressure on fiscal deficits and with the US close to passing a budget that will significantly add to their government deficit, long term debt will be scrutinised as to how sustainable countries deficits are.

Inflation concerns have also eased, apart from possibly in the US where tariffs have yet to make their impact. In Europe inflation is now back to 2% and, following the hike created by utility bills/council tax/employment costs, should ease in the UK (helped by a weaker dollar) allowing the Bank of England to cut interest rates further. In the US some tariffs increases and disruption to supplies are leading to higher prices, but until trade deals are struck we won't know the full impact. Oil, which can have a significant impact on inflation, jumped in price when Israel and Iran exchanged aerial attacks, but quickly fell back when a ceasefire was agreed.

The lesson from the first half of the year is that keeping a cool head will definitely have served you better than knee jerk reactions to febrile politics and armed conflict. We will keep your investments well diversified and carefully watch that valuations don't embed too rosy an outlook!

OPEC+ continues to raise production quotas, with the price of oil currently settled around the high $60s per barrel. The market looks well supplied into 2026, but is obviously sensitive to Middle East hostilities. European gas prices have also eased helping the inflation outlook, of which energy is a large component. Industrial metal prices slumped on the introduction of US tariffs, only partially recovering on their deferral. Gold has surged on the back of tariff uncertainty, geopolitical tensions and moves by central banks to diversify their reserve holdings away from the US dollar. Food prices might create some problems this year; notably in Japan the price of rice doubled in the first half of the year.

Global supply chains have improved significantly after a long period of disruption, but not back to the level of efficiency pre- Covid. The worry is that tariffs will again disrupt the global supply chain and lead to shortages of some critical components. China has become the dominant supplier in a number of crucial areas, such as rare earth metals where they control ~90% of global processed supply and have already been restricting shipments.

A global interest rate cutting cycle (bar Japan) is still in place. Although there are different views on the pace and extent of cuts, they will help small companies' finances and households with mortgages. The yields on long bonds have declined, on economic growth concerns, but remain sensitive to the growing levels of government debt across the western world. Along with tariff uncertainty, this continues to act as a headwind against long term investment decision taking.

Property fund mergers in 2024 have been followed by a significant number of takeovers for property REITs as their large discounts to underlying asset value has attracted international interest. With rents continuing to rise and vacancy rates at low levels, property still looks attractive, if share price discounts remain. Listed infrastructure trusts also trade on wide discounts, renewable energy focused ones still face uncertainty on energy prices, but new regulations should provide more certainty on long term power pricing. Despite windfall taxes and higher debt costs there is still plenty of room to grow.

Political policy continues to be fluid, with plenty of U-turns both here and abroad, as well as recent election surprises in Poland, S Korea and Holland. The clear shift towards nationalist politics was countered, to an extent, in the German election, creating a right of centre government that has enabled a large fiscal spending package. In the US the Trump administration has unleashed a raft of executive orders, affecting both national policy as well as international, through tariffs. The US budget is the current piece of legislation that has markets' attention.

Despite flirting with technical recessions (two successive quarters of economic contraction) in Europe a full-on recession has so far been avoided; the fabled 'soft-landing'. However, supporting economies through Covid and the energy price spike have a real cost and take away from other economic activity; meanwhile the tricky issue of how to fund greater levels of defence spending will need to be addressed. Softness is now beginning to emerge in the employment market, although real wages have grown after a long period of erosion and a rise in household savings means consumer finances are generally quite healthy.

Company results from the first quarter of 2025 held up well in general, with aggregate reported profits moving ahead. Second quarter results will soon be reported with some tariff impacts, however, there is considerable uncertainty as to whether it will be tariff bark or bite in the second half. AI continues to be a strong structural growth driver. Consumers have been showing greater price sensitivity and some industrial companies have reported demand weakness, this is particularly true of car companies, who have been slashing their forecasts.

Despite the current ceasefire between Israel and Iran, conflict continues to rage elsewhere, and lasting peace feels some way-away. This has led to a substantial policy shift in Europe, with recognition that there will need to be a significant increase in defence spending, to 'be prepared'. Some companies will be beneficiaries of this, but with spending cuts elsewhere needed to try and balance the books, there will also be losers. Looking through all the uncertainty we still see positive investment returns, but expect bumps along the way.

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Market Outlook

Equities	Despite wars and tariff turmoil stock markets finished the first half of the year at or close to record highs. A ceasefire, currently holding, between Israel and Iran and a lower oil price have helped. The UK's limited trade deal with the US is now in effect, but we await the 9th of July to see if other deals are struck, or the US imposes unilaterally. Although companies are expected to report limited impacts from US tariffs from the second quarter, there are reports of supply disruptions and uncertainty as to what the second half will hold.
Fixed Interest	Enthusiasm for interest rate cuts cooled in the US with the economic uncertainty and inflationary potential created by tariff proposals, meanwhile the Bank of England cut the base rate by a quarter of a percent in May. Better than expected Q1 GDP and higher than expected April inflation have paused UK rate cuts , but further cuts are expected later this year. Long term bonds (10 years +), however, have to contend with forecasts of rising government deficits, so steeper yield curves can be expected.
Commercial Property	There has been a marked pick-up in M&A activity in property trusts (REITs), as market stabilisation and steep discounts to quoted asset values have attracted takeover offers. This has probably been aided by a growing consensus that debt costs (one of the key factors in valuing property) have stabilised. Supply and demand have settled down and with limited new build, and higher energy standards required, the market looks to be well underpinned.
Alternative Assets	Infrastructure investment funds offer benefits for exposure to physical assets, some with attractive inflation linked contracts, and growth tied to improved connectivity and de-carbonising economies; although build costs have risen. High debt costs, that weighed on the valuations of private equity and infrastructure trusts, remain an issue but de-gearing is taking place. Absolute Return strategies have shown some defensiveness but generally offer low returns and we continue to choose sparingly.
Cash	The investment return on cash and cash like instruments has peaked and is expected to gradually decline through this year.

Thorntons Investments **2nd July 2025**

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