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INVESTMENT MEMORANDUM

This review was largely completed before President Trump announced a significant, but not total, retreat from his 2nd April tariff announcements and markets have, accordingly, seen a large relief rally. Given how fast events are moving, we do not plan to change what we have written which largely relates to the malign effects of tariffs and perhaps, which is probably what caused President Trump to backtrack, the powerful restraining effect of the bond market.

Given the 2nd April announcement by President Trump of sweeping tariff levies on imports into the USA, the portfolio review, performance figures and tables for Q1 2025 seem academic now given the hugely negative effect which his announcement has had on markets. The review which follows the “Market” section goes into more detail about the economic consequences of the levy and what it might mean for investors. The tariffs represent an egregious act of self harm to the US economy and similarly for the rest of the world. There is no economic theory which can seriously justify tariffs on this scale and there is no doubt that, unless rescinded quickly, they could lead to a world recession or, at best, a slowdown in economic growth to near zero.

President Trump is unpredictable but tariffs have been an obsession of his for a long time and, as this is written, he shows no sign of reversing his 2nd April announcement. What could make him change his mind? One of the most important constraints on politicians is the bond market. The US borrows a lot of money because of its outsize budget deficit (US\$1.83 trillion in 2024) and its very large level of outstanding public debt as a percentage of GDP (c. 124%), so it is important. We have quoted in this review in the past the words of James Carville, an advisor to President Clinton, but they are worth quoting again. He said “I used to think that if there was reincarnation, I wanted to come back as the President or the Pope or as a .400 baseball hitter. But now I would like to come back as the bond market. You can intimidate everybody”. The US dollar does, of course, have the advantage of being the world’s largest reserve currency but, if there is a loss of confidence in the USA, say by foreign holders of US Treasury bonds (they own nearly a quarter), that could concentrate the President’s mind. 30 year Treasury bond yields have moved up sharply. Then there are the voters. With mid term elections next year Republicans in the Senate and the House of Representatives will already be very nervous. Whether the President, in his second term, would heed their concerns is unknown but he might given the swing in public opinion already occurring. Then within Congress there are moves to try to stop the tariffs and there is some cross party support in the Senate. It’s possible the issue could end up at the Supreme Court but this is uncharted territory. The pressure from big business and Republican donors is already strong and is likely to get stronger.

What does it mean for investors? We have seen extraordinary market volatility. To be clear here, although the President’s views on tariffs were well known, the magnitude came as a shock and was not discounted by investors. As our clients will know, we never respond with kneejerk reactions to unexpected events. History shows that those who sell out in response to bad news usually regret it, the worst recent occasions being the Covid outbreak when sharp losses were more than recovered by the year end.

As our detailed review shows, we do not think the current situation makes the case for bonds. Recession or negligible growth will worsen governments' finances and tariffs are likely to increase the inflation rate. There will be concerns about some countries' credit ratings or even creditworthiness. High quality equities are likely to be on safer ground. Companies' profits will be affected in many cases but not so much that it significantly affects their dividends or their chance to recover their growth path when the current uncertainty ends. The US has been our favoured area. We will review everything when things calm down. We highlight some economic risks for the UK which reinforce our belief that significant non UK exposure remains prudent as it has done in the past as far as returns are concerned.

The tables below detail relevant movements in markets to the end of March (although now overtaken by subsequent events):

International Equities 31.12.24 - 31.03.25

Total Return Performances (%)				
Country	Local Currency	£	US\$	€
Australia	-3.0	-5.3	-2.4	-6.5
Finland	+9.8	+11.2	+14.6	+9.8
France	+5.7	+7.0	+10.3	+5.7
Germany	+10.9	+12.3	+15.7	+10.9
Hong Kong	+3.7	+0.5	+3.6	-0.7
Italy	+12.6	+14.0	+17.4	+12.6
Japan	+3.9	-2.1	+1.0	-3.2
Netherlands	-2.4	-1.2	+1.9	-2.4
Spain	+17.2	+18.6	+22.2	+17.2
Switzerland	+9.0	+8.3	+11.7	+7.0
UK	+5.4	+5.4	+8.6	+4.1
USA	-4.3	-7.2	-4.3	-8.3
All World Europe ex UK	+6.4	+7.6	+10.9	+6.3
All World Asia Pacific ex Japan	+1.0	-2.1	+0.9	-3.2
All World Asia Pacific	-0.7	-2.1	+0.9	-3.3
All World Latin America	+7.9	+10.7	+14.1	+9.3
All World Emerging Markets	+2.0	-0.8	+2.2	-2.0
All World	-1.9	-4.0	-1.0	-5.1

Source : FTSE All World Indices

FTSE UK Government Securities Index All Stocks (total return) : +0.6%

International Bonds - Benchmark Ten Year Government Bond Yields (%)

Currency	31.12.24	31.03.25
Sterling	4.56	4.67
US Dollar	4.57	4.19
Yen	1.07	1.49
Germany (Euro)	2.36	2.74

Sterling's performance during the quarter ending 31.03.25 (%)

Currency	Quarter Ending 31.03.25
US Dollar	+3.2
Canadian Dollar	+3.3
Yen	-1.7
Euro	-1.2
Swiss Franc	+0.6
Australian Dollar	+2.3

Other currency movements during the quarter ending 31.03.25 (%)

Currency	Quarter Ending 31.03.25
US Dollar / Canadian Dollar	-0.1
US Dollar / Yen	-4.7
US Dollar / Euro	-4.3
Swiss Franc / Euro	-1.7
Euro / Yen	-0.5

Significant Commodities (US dollar terms) 31.12.24 - 31.03.25 (%)

Currency	Quarter Ending 31.03.25
Oil	-0.5
Gold	+17.7

MARKETS

The movements in the FTSE All World indices over the quarter, -1.9% in local currency terms, -4.0% in sterling terms, -1.0% in US dollar terms and -5.1% in euro terms, belie some sharply divergent movements in the underlying country and regional indices. In a sharp reversal of recent trends, the US market underperformed by a distance the Europe ex UK Index markets as well as that of the UK. The US tech sector, previously so strong, underwent a sharp reversal of fortunes, whereas more defensive stocks, often seen in Europe, came into their own.

Our table also demonstrates the effect of currency movements during the quarter. The weakness of the US dollar reduced returns further in US dollar denominated assets for many overseas investors, including sterling based ones, but sterling based investors in euro denominated assets saw their returns enhanced.

As our table shows, there was a sharp divergence in bond performances over the quarter when looking at ten year government bonds. Whilst gross redemption yields rose, and therefore prices fell, in three of the four markets reported in our table, the US dollar bond market was a notable exception with the gross redemption yield on the ten year bond falling sharply by 38 basis points. As this review is finalised on 12th April, we can note that the 10 year UK government bond yield is 4.74%, the US Treasury bond is 4.38%, the German Bund is 2.60% and the Japanese Government Bond is 1.25%. There has been some serious weakness in the 30 year UK government bond as the yield curve has sharpened.

In the currency markets, as alluded to above, sterling rose against the US dollar and Canadian dollar as well as the Australian dollar and, to a lesser extent, the Swiss franc, but it weakened against the yen and euro.

In the commodity market, gold regained its status, in what many would say was its historical role, as a store of value in uncertain times, rising by 17.7% over the quarter.

ECONOMICS

There have been so many developments since we started to write this review towards the end of March that it has required a considerable rewrite in view of the events of 2nd April when President Trump announced his tariff proposals. We had started by saying that it was important to play the ball and not the man, given the strong emotions which President Trump elicits in people, and to see what he does rather than what he says. His “beautiful” tariffs shocked economists and investors because although tariffs were expected, they were on a scale well above what most had imagined, hence the shockwaves in markets because they had not been discounted. In our first draft of this review, we had discussed what investors might consider positive developments since he became President and potential negative ones of which potential tariffs were at the forefront. We always try to look at various governments’ policies through the eyes of an investor since whether we agree or disagree with them is not relevant. It is the effect which they may have on markets which is what concerns us.

However, as an exception, we must say why, and our clients reading this will appreciate the reasons, his tariff announcement represents, as we said at the beginning of this review, an egregious act of self harm for the US economy and the rest of the free world. The thinking behind the idea of tariffs as applied is very seriously flawed. To be objective, President Trump is not wrong in saying that the USA has faced some discrimination from its trading partners but to announce the level and extent of tariffs which he has defies reason and one would have thought the consequences should easily have been apparent to him and his team. The theory of comparative advantage, stated very simply, says that a country with a comparative advantage in providing a certain good will export that product and import the good in which another country has a comparative advantage. So, for example, a low cost country will have a comparative advantage in producing low value added goods but another high cost country might have a comparative advantage in producing, say, a capital goods product. The idea behind President Trump's tariffs is that those countries enjoying a trade surplus with the USA should be penalised with high tariffs. It is inevitable that the USA will suffer a trade deficit with some countries which enjoy an overall comparative advantage in what they produce and sell to the USA and therefore have a bilateral trade surplus and vice versa where the USA has a competitive advantage and a trade surplus. The idea that trade should be balanced with every country with which the USA trades has no economic merit. Furthermore, the mechanics behind the way the tariffs are calculated also have no economic merit. Taking the trade deficit with its counterpart as a percentage of imports into the USA and dividing the result by two lacks any economic logic. The President says that other countries are ripping off the USA, or words to that effect, but the fact is that the USA is consuming far more than it is producing, hence the current account deficit. Were the USA to consume less, the imbalance would improve. At the moment, the USA has an important reliance on foreigners to acquire its debt and, as stated earlier, this could be one of the influences which forces a change of policy in the President.

It is worth spelling out, because of the investment implications, what the effects of President Trump's tariff impositions might be. These are so obvious, that it is hard to believe that the President and his advisors ignored them. He basically wants an outcome which will lead to massive import substitution but ignores the fact that the USA is a high cost country so the manufacture of many imported goods will not be viable. Another obvious consequence is that tariffs will raise prices which will feed through to the consumer price indices. If the Federal Reserve becomes concerned about the inflation level, the expected further cuts in interest rates may not materialise and it is possible that cuts already made will be reversed. This and the fact that consumers' disposable incomes will be adversely affected will dampen economic activity in the USA. Furthermore, on the inflation front, domestic US producers will lose a spur to efficiency because price competition is reduced so prices of some domestically produced items may rise anyway. On the other side of the coin, countries which retaliate by placing tariffs on US imports will mean lower volumes of US exports to them and lower economic activity. With these trade barriers in place, world economic growth will slow down, quite possibly causing a recession, the economic effects of which will be malign in terms of employment, economic activity and governments' finances as tax takes are adversely affected and expenditures rise due, in part, to higher unemployment. One of President Trump's arguments is that money raised through tariffs will help tackle the USA's enormous budget deficit, (US\$1.83 trillion), running at nearly 7% of GDP and finance tax cuts which he proposes. The Treasury Secretary says they could bring in anywhere between US\$300 billion and US\$600 billion with independent estimates at the lower end of the range or even lower. The likely effects of a world economic slowdown, or possibly recession, will be to make budget deficits worse. That does not only apply to the USA, which still has some, but now probably diminishing, advantage as the world's largest reserve currency, but to countries like the UK, France and Italy to name some nearer home. This would threaten the credit ratings, if not the credit worthiness, of some countries. As this is being written, sterling has come under some pressure. As a particularly open economy, the UK has a greater degree of vulnerability than most even though UK exports to the USA will attract the lowest tariff rate, 10%, except for motor, steel and aluminium exports which will suffer the 25% tariff. The gearing effect on governments' finances arising from a slowdown in economic growth or even recession is significant as we saw from the

UK's OBR reduction in its March projections for UK growth this year and the effect which it forecast on government finances and through that to taxation and public spending. It is important to dwell on this for a moment because, as a result of the mayhem caused by President Trump's tariff proposals, investors have moved to shorter maturities of bonds as a supposedly safe haven. But insofar as the tariff measures threaten government finances for the reasons given and through that to a downgrading of some countries' credit ratings, it poses a threat to the bond markets in general and to countries with vulnerable finances in particular. Even if the tariff measures were rescinded tomorrow, what has happened cannot be undone in terms of the perception of the USA as a trading partner or, in the political sense, as a reliable ally, perhaps the latter notably in the area of defence. Trade patterns are bound to change as countries seek to reduce their reliance on the USA. Supply chains are very delicate links in the manufacturing process and companies will want to reduce vulnerabilities such as those introduced by the sudden imposition of tariffs.

Whilst tariffs are inevitably dominating the news because of the effect which they have had on the international equity markets, investors should not lose sight of the other policies President Trump has adopted, some of which investors might regard as positive and which have also been taken up by other governments as they seek to tackle their economic problems. It might seem particularly relevant to what is happening in the UK. One of the economic issues which many governments are facing is how to control the growth of public expenditure. There are various ways in which governments might try to do this and two of the ways it has chosen to follow, although to a different degree, reflect what has been happening in the USA. President Trump appointed Elon Musk to reduce the size of the USA's equivalent of the Civil Service, through DOGE (the Department of Government Efficiency). This has meant the loss of many government roles and departments as he has made attempts to reduce the cost of government, one of the ways to tackle the USA's outsize budget deficit. The UK's plan is much milder but follows a form of what has been happening in dramatic style in the USA as it seeks spending savings. The second area is deregulation, something we have often written about in recent reviews before it came to the fore with President Trump's deregulation agenda, and that investors will read as a positive development. In many countries and regions, regulations have grown exponentially, the USA, UK and EU to give three examples. A fully functioning economy will have regulations proportionate to the area under regulation but no more. Regulations impose costs and, if unnecessary, slow down economic growth as they impose an expensive dead weight for businesses. President Trump has pursued deregulation with vigour and, if tackled properly, it can result in a cost free economic stimulus. As the UK struggles to stimulate economic growth, the deregulation policy has been borrowed enthusiastically from the USA in various areas, such as ordering the various regulators to regard economic growth as one of their prime mandates, reviewing the necessity for so many regulators and loosening planning laws, to name some initiatives. We have in reviews last year focused in the UK on the CMA (Competition and Markets Authority) which had been quite aggressive in its review of mergers and also towards the US technology companies, something which President Trump noted. The Chairman of the CMA has stood down and the noises coming from the CMA seem to suggest that the Chancellor's deregulation message has been taken on board. In the EU, whilst change generally comes slowly because so many countries have to agree, there appears a gradual realisation that they have to contain regulation in order to encourage economic growth. Mario Draghi's report last year highlighted this necessity.

Another strong statement affecting Europe has come from President Trump in the area of defence. He has left no doubt that the continent has to look after itself and cannot necessarily look to the USA for defence if under attack. This has been brought into relief by the Russian invasion of Ukraine. He has been successful in initiating a sharp rise in NATO countries' defence spending at a time when public finances are stretched. The most dramatic effect is in Germany where the constitutional debt brake has been relaxed enabling a large increase in defence spending and a €500 billion infrastructure spend. Besides the political importance of this, the economic implications are relevant since, because of Germany's strong credit rating arising from its relatively low level of outstanding public debt as a percentage of GDP, it can afford this and, importantly, provide an economic stimulus to the country which might spread to other EU countries. Because Europe will be more reluctant to buy US

weapons, it will accelerate further development of the European defence industry. However, one other economic effect in the eurozone is not likely to be so welcome. Before the 2nd April tariff announcement, eurozone bond yields had risen sharply on the back of this news from Germany because German government bond buyers had anticipated higher levels of German government borrowing. As the eurozone's best credit, other governments' bonds trade off German yields so theirs rose also. As mentioned earlier, post 2nd April, bond yields of some maturities fell and prices rose being a kneejerk reaction to the perceived flight to safety. However, when we see a more normal situation, investors are likely to consider what lower economic growth is likely to mean for eurozone governments' finances and view it in the context of their budget deficits and outstanding levels of public debt as a percentage of GDP.

Our clients, being sterling based, will be sensitive to the movement in sterling and what happens in the UK. As clients know, we regard the UK as just one market in which to invest and do not give it any special preference as the accounting currency of a portfolio. It is nowadays a relatively small market accounting for between 3% and 4% of the FTSE All World Index and we have always had a heavy weighting outside the UK, mainly in the USA, because we have not felt it to be a relatively attractive market. As this is written, we are in a fast moving situation, but an inkling of the canary in the mine is the weakness of sterling in the past few days. The UK economy is in a difficult position and investors can be forgiven for a degree of confusion about economic policy. The government is trying to pull as many levers as it can to stimulate economic growth and can point to announcements in that direction; we mentioned deregulation earlier and its instructions to regulators to give a high priority to economic growth in formulating their actions. There is also the relaxation of planning rules because stimulating housebuilding is one of the easier wins if the capacity is there to increase significantly the rate of housebuilding. Recent announcements of indications of approval of airport expansion at Gatwick and Heathrow and the Transport Secretary's overruling of the planning inspectors recommendation not to allow expansion at Luton Airport speak to this. On the other hand, investors will see the opposite effect arising from the coming into operation in April of the big increase in employers' National Insurance contributions, together with the lower limit at which they apply, a sharp rise in the minimum wage, and the forthcoming Employment Rights Bill which will increase the costs and risks for business. Because of the deterioration in the international economic outlook arising from President Trump's tariffs, it is likely that the headroom allowed for the Chancellor in 26th March statement in terms of keeping within her self-imposed borrowing limits will disappear again necessitating either cuts in public spending, increased taxes or both. Although the UK has been hit with the minimum tariff levels applied by President Trump and therefore has some relative advantage against the EU for example, it will be adversely affected in terms of economic activity. Jaguar Land Rover has suspended exports of the US for a month. The government is going to have to make some difficult decisions, probably in the area of public spending including on welfare which has risen so fast. The foreign exchange and bond markets will instil discipline on the UK's finances as they will elsewhere. So, whilst the UK market has many defensive stocks, the country's finances are in a difficult situation and signalling is very important. So, investors will see mixed signals in terms of policy as described above and also in terms of attitude to wealth. The ending of non domiciled status and the exodus of wealthy people, whilst satisfying political imperatives, sends out a negative signal about the UK's attitude to wealth and might be seen to be an act of self harm. Whether one agrees or not about such policies, the message for investors in the UK is unmistakable.

The US tariffs for the EU have been set at 20% and provide a very difficult dilemma for the area. In 2024, the EU exported €531.6 billion in goods to the USA and imported €333.4 billion resulting in a trade surplus of €198.2 billion. The EU talks about retaliation but this could be dangerous if it results in the USA increasing tariffs against the area as it has with China. Furthermore, given the tariffs being levelled or threatened against China by the USA, it is quite possible that the EU will see some diversion of Chinese exports to the EU from the USA causing further pain to industries like the car industry. But our concern about the EU is the level of indebtedness in some eurozone markets both current in terms of the budget and, overall, in terms of the outstanding level of public debt as a percentage of GDP. In this context, what happens to the political impasse in France will be important.

With a budget deficit of around 6% of GDP, the polarisation of the French parliament following the last elections makes it difficult to get to deal with the situation. The relatively poor performance of the French stock market in 2024 shows that politics does matter in markets. The budget for 2025, passed in February, was formulated to help to contain the country's budget deficit to 5.4% of GDP. In the case of the UK, which we discussed above, signalling is important for investors. Major French companies will have to pay an exceptional surtax on their profits. Their tax will increase by 20.6% or 41.2% depending on the scale of their total sales revenue for one year only. There are other measures which will hit businesses but the signalling is clear and investors will not find it encouraging. Because the size of the French state is so large and the difficulty of tackling it without inciting social unrest so immense this is a situation which investors will be watching. Not since the 1970s has France managed to balance its budget. Because of the currency union, problems in one country can be hard to isolate and this is always a potential concern about the eurozone.

And then there is China which seems the main focus of President Trump's ire as the tit for tat continues. China has retaliated against the US's latest tariff increase to 104% by raising its tariffs on US imports to 84% and there have been subsequent further developments. The domestic policy reaction in China was for the central banks to loosen its grip on the yuan to boost exports and promise more loans to stabilise the market as it has headroom to borrow more. As well as a domestic stimulus, Chinese companies, as we said in relation to the EU, will likely divert sales. A longer term problem for China is an acceleration of a trend by foreign companies to move production away from China to countries which, although facing US tariffs, very high ones in some cases, may be less in the USA's crossfire. This was already happening before the latest events. Supply chains will be reassessed, a logical reaction to what has been happening.

So, we are in a fast moving situation and by the time this review goes out to our clients, we may be in a different situation such is the unpredictability of the US President. Whilst it seems that nothing will move him to backtrack given his obsession with tariffs, no one is bigger than the markets and James Carville's comments at the beginning of this review may become particularly relevant in terms of what will cause him to change his mind on tariffs. To confirm our view, at this moment in a fast moving situation, we see bonds facing significant headwinds whilst equities, despite their battering have the better fundamental attractions. Above all, as on occasions previously when markets have taken an unexpected fall, we have not been intimidated into selling good shares by the febrile state of the markets.

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